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In The

Supreme Court of the United States

October Term 1995

COST CONTROL MARKETING & SALES MANAGEMENT OF VIRGINIA, INC.; WILLIAM P. PETERSON; ARTHUR KUJAWSKI; RICHARD R. COSTENBADER; JAMES M. MARLEY,

Petitioners,

v.

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT,

Respondent.

Petition for Writ of Certiorari

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

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HIP

I. STATEMENT OF QUESTIONS PRESENTED

1. Shall the word "developer" as used in the Interstate Land Sales Full Disclosure Act be construed to encompass anyone who buys or sells lots in an eight year old completed subdivision?

2. Is an award of civil restitution exempt from discharge pursuant to 11 U.S.C. § 523(a)(7)?

3. In a civil action, may an individual be held liable without evidence?

4. In an administrative enforcement action, may the ultimate burden of proof as to damages be shifted to the defendants after an initial proffer of hearsay by the Government?

5. May an individual be ordered to disgorge moneys he never received?

II. PARTIES

The parties to this petition are Cost Control Marketing and Sales Management of Virginia Incorporated (CCMV), William P. Peterson, Arthur Kujawski, Richard R. Costenbader and James M. Marley.

The parties in the Courts below were, in addition to those parties named above, Thornton Byron, Stuart Guskind, Earl Hissom, Monticello Development Corporation (MDC) and the United States Department of Housing and Urban Development, (HUD).

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V. PRIOR OPINIONS

The prior opinions issued by the Courts below in the instant proceeding have all been published and are cited as follows: Kemp v. Peterson, 940 F.2d 110 (4th Cir. 1991), Kemp v. Cost Control Marketing & Sales Mgm't, 790 F. Supp. 1274 (W.D. Va. 1992), Cisneros v. Cost Control Marketing & Sales Mgm't, 862 F. Supp. 1531 (W.D. Va. 1994), United States Dep't of Housing and Urban Development v. Cost Control Marketing & Sales Mgm't, 64 F.3d 920 (4th Cir. 1995).

VI. JURISDICTION

Petitioners seek this Court's review of the judgment entered on September 8, 1995 by the United States Court of Appeals for the Fourth Circuit, to which a petition for rehearing and suggestion for rehearing en banc were denied by that Court's order of November 3, 1995, by a Petition for Writ of Certiorari pursuant to the jurisdiction conferred by 28 U.S.C. § 1254(1). This Petition is timely filed because it was mailed within ninety days of November 3, 1995, the date of the denial of the petition for rehearing. Rules 13.4 and 29.2.

VII. STATUTES INVOLVED

11 U.S.C. § 523:

> (a) A discharge under section 727, 1141, 1228(a), 1228(b), or 1328(b) of this title does not discharge an individual debtor from any debt --

. . .

> (7) to the extent such debt is for a fine, penalty, or forfeiture payable to and for the benefit of a governmental unit, and is not compensation for actual pecuniary loss, other than a tax penalty --

. . .

15 U.S.C. § 1701:

For purposes of this title, the term --

. . .

> (5) "developer" means any person who, directly or indirectly, sells or leases, or offers to sell or lease, or advertises for sale or lease any lots in a subdivision;

. . .

VIII. STATEMENT OF THE CASE

Procedural History

This action was commenced by the filing of a Complaint on November 15, 1989, by the plaintiff, the U.S. Department of Housing and Urban Development ("HUD"). (A81-A97) The Complaint named as defendants Cost Control Marketing and Sales Management of Virginia, Inc. ("CCMV"), and William P. Peterson, Arthur Kujawski, Richard R. Costenbader and James M. Marley (collectively hereinafter, the "Individual Defendants"), the Petitioners herein. (A81) Also named in the Complaint were Thornton Byron, Stuart Guskind, Earl Hissom and Monticello Development

Corporation, ("MDC"). (A81) Served with the Complaint was a Motion for a Preliminary Injunction. (A93) A Preliminary Injunction was entered by the District Court on February 14, 1990. (A16)

On February 20, 1990, CCMV filed a Motion for Summary Judgment, and on February 21, 1990, CCMV filed a Motion to Strike Count III of the Complaint. On March 9, 1990, HUD filed a Motion for Partial Summary Judgment on Counts I and II of the Complaint.

On March 16, 1990, the Individual Defendants noted an appeal to the U.S. Court of Appeals for the Fourth Circuit from the Preliminary Injunction.

On May 18, 1990, the District Court entered an order denying CCMV's Motion for Summary Judgment and Motion to Strike, and granting HUD's Motion for Partial Summary Judgment.

On May 21, 1991, HUD filed a Motion for Summary Judgment on Count III of the Complaint and For Entry of Judgment on all Counts against the Individual Defendants.

On August 2, 1991, the Fourth Circuit issued its opinion regarding the Individual Defendant's appeal of the Preliminary Injunction, and remanded the case for factual findings to support the asset freeze. Kemp v. Peterson, 940 F.2d 110 (4th Cir. 1991). (A22-A30) On November 11, 1991, the District Court held a hearing pursuant to the Fourth Circuit's order of remand.

On April 22, 1992, the District Court entered the Interim Judgment Order, which granted HUD's Motion for Summary Judgment on Count III of the Complaint, and ordered interim relief as to all counts. (A31-A45) On May 11, 1992, the Individual Defendants

noted their appeal of the Interim Judgment Order to the Fourth Circuit. On June 22, 1992, the Fourth Circuit dismissed the appeal without prejudice to the filing of a subsequent appeal once all matters had been made final.

On July 20, 1992, defendants Marley[1], Peterson[2] and Costenbader[3] filed for bankruptcy protection in the U.S. Bankruptcy Court for the Middle District of Pennsylvania. Inclusive in each filing was the District Court's April 22, 1992 judgment. On January 7, 1993, defendant Marley received a discharge in bankruptcy. The stay created by these bankruptcy filings was never filed by HUD even though HUD was ordered by the court to do so. (A51-A52) Defendants Costenbader and Peterson were discharged in bankruptcy on January 15, 1993. The Marley and Peterson cases were never closed, and are still open. Defendant Costenbader's case was reopened on motion of the debtor on January 28, 1994.

On January 7, 1994, HUD filed a Motion for Final Judgment and for Sanctions. On July 27, 1994, Magistrate Crigler filed his Report and Recommendation concerning final judgment. (A53-A61) On August 8 and August 12, 1994, CCMV and the Individual Defendants, respectively, filed their Objections to the Magistrate's Report. On September 15, 1994, the District Court entered an order overruling the defendants' Objections to the Magistrate's Report and entering final judgment. (A73-A76)

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[1] Case No. 5-92-01299
[2] Case No. 5-92-01300
[3] Case No. 5-92-01301

Factual Summary

During the entire five-year span of this litigation, not one witness ever took the stand, and not one piece of evidence was ever introduced in open court. Instead of relying upon admissible evidence, HUD filed declarations and affidavits. (A81) Due to the nonexistence of evidence in this matter, it is impossible to give citations to the record for the summary given below. The following facts, offered to the District Court below in a memorandum, are substantially uncontroverted.

In 1968, defendant Monticello Development Corporation ("MDC"), purchased land surrounding Lake Monticello in Fluvanna County, Virginia. MDC developed the land into a subdivision (known as Lake Monticello Subdivision, hereinafter the "Subdivision"), consisting of 4,592 lots, and by 1978 had sold 4,540, or 99%, of those lots. (A3) During its sales effort, MDC had fully complied with the registration and other requirements of the Interstate Land Sales Full Disclosure Act, 15 U.S.C. § 1701, et seq., (the "ILSFDA"). By year end 1978, MDC had fully constructed the Subdivision and had improved it with roads, utilities, club house, marina, lakes, picnic areas, tennis courts and other amenities.

Defendant Cost Control Marketing and Sales Management of Virginia, Inc. ("CCMV") was organized as a Virginia corporation in 1986. At all times relevant herein, defendants Peterson, Kujawski, Marley and Costenbader (collectively, the "Individual Defendants"), were, respectively, the president, vice president,

secretary/treasurer and Chief Executive Officer of CCMV.

CCMV was organized for the sole purpose of acquiring Lake Monticello lots from the general public, placing them into inventory, and re-selling the lots to new buyers. In all, CCMV purchased 919 vacant lots at the 4592 lot Subdivision from August 1986 to July 1989. (A3) CCMV made no improvements to its lots. Between May 1987 and December 1989, CCMV sold 585 lots from its inventory. In no instance did CCMV undertake to do any other activity within the Subdivision other than to inventory its 919 lots and thereafter market and sell them.

CCMV admitted it made no effort to comply with ILSFDA. Rather, it is CCMV's position that MDC and not itself is Lake Monticello's sole developer, and accordingly, compliance with ILSFDA by neither CCMV nor any other lot owner in the Subdivision was not required.

There is no evidence in the record to indicate that the Individual Defendants ever themselves engaged in the sale of lots in the Subdivision. The record establishes that the Individual Defendants were officers of CCMV, and nothing more. There is no evidence that any of the Individual Defendants ever received so much as one cent from the proceeds of CCMV's sales of lots in the Subdivision. There is no evidence in the record that any of the Individual Defendants engaged in any acts tantamount to "aiding and abetting" CCMV in any allegedly illegal activity. There is no evidence in the record which serves as a factual predicate for the liability of the Individual Defendants upon any theory. Other than establishing the

Individual Defendants' status as officers of CCMV, the record is completely silent as to any of their alleged acts or omissions.

The District Court ruled CCMV to be a developer within the ILSFDA and liable therefore and also held the Individual Defendants jointly and severally liable for $8.6 million, which the District Court adjudicated as nondischargeable in bankruptcy. (A73) No trial was ever had. During the entire five year span of this litigation, not one witness ever took the stand. Not one exhibit was ever introduced into evidence in open court. No Individual Defendant ever appeared in person before the Trial Judge. All matters were adjudicated upon motion for summary judgment, with grossly inadequate evidentiary support.

The Fourth Circuit affirmed the District Court's ruling in all respects. (A1)

IX. ARGUMENT

A. The Petitioner CCMV was not a "Developer" within the meaning of the Interstate Land Sales Full Disclosure Act.

The Interstate Land Sales Full Disclosure ("ILSFDA") was not designed to regulate the on-going resale of lots within a subdivision completed almost eight years earlier. The legislative history of the ILSFDA makes clear that the ILSFDA was designed to regulate the original developers who sell lots in an incomplete subdivision.

The ILSFDA was passed by Congress as Title XIV of the Housing and Urban Development Act of 1968 and became effective

on April 28, 1969. It imposed a comprehensive federal regulatory framework upon the real estate development industry. The Act was passed to prevent "false and deceptive practices in the sale of **unimproved** tracts of land by requiring developers to disclose information needed by potential buyers." Anders v. Dakota Land and Development Co., Inc., 380 N.W.2d 862, 865 (Minn. App. 1986) (emphasis added); Flint Ridge Development co. v. Scenic Rivers Association of Oklahoma, 426 U.S. 776, 778, 96 S.Ct. 2430, 2433, 49 L.Ed.2d 205(1976). The situation that the ILSFDA is designed to prevent is aptly described in McCown v. Heidler, 527 F.2d 204 (10th Cir. 1975):

> The 'developer' of a land sale plan is usually a corporate entity which, in a fraudulent scheme . . ., ends up defunct and offers no reserve for recovery to those persons defrauded; so, too, the end selling agent, when the development collapses financially, is often long gone or cannot respond pecuniarily.

The legislative intent in passing the ILSFDA was to advise potential buyers, in writing, what the developer promises for a subdivision upon its completion. The ILSFDA's remedial measures afford purchasers recourse should the developer fail to complete the development as represented at the time of purchase.

Obviously, the ILSFDA has a prospective view; the potential buyer does not need disclosure of the features of a completed

development, for the subdivision in place speaks for itself. The ILSFDA's focus was to advise the potential buyer of what the developer promised in an incomplete subdivision.

Since the adoption of ILSFDA, several circuits have interpreted "developer" to include and exclude certain entities depending upon the circumstances at hand. Unlike the District and Circuit Courts in the instant case, these cases have disregarded the strict interpretation of "developer" by considering the circumstances of the case. The District Court's ruling, with the Fourth Circuit affirming, has resulted in a split among the Circuits holding different views on the issue. Only the Fourth Circuit appears to follow the narrow interpretation of "developer" in holding CCMV subject to the ILSFDA because it sold a lot in Lake Monticello without regard to any extenuating circumstances such as from whom title was obtained, the number of lots involved, the method of sale, and participation by the owner in activities within the subdivision. The Fourth Circuit represents the minority view.

The Tenth Circuit applied an opposite interpretation to "developer" by considering extenuating factors and circumstances. This is the majority view. In McCown v. Heidler, 527 F.2d 204 (10th Cir. 1975), the meaning of developer was expanded to include aiders and abetters and controlling stockholders and directors who were behind the corporate bankrupt subdivider. The Third Circuit by inference followed McCown in Bartholomew v. Northampton Nat. Bank of Easton, 584 F.2d 1288 (3rd Cir. 1978) holding that in the

absence of any allegation either that banks involved in the financing or that the sole equitable owner sold, offered to sell or advertised for sale any lots in the subdivision or that they performed any such activities through agents or other means were not developers within the meaning of ILSFDA. See also, Adema v. Great Northern Development Co., 374 F. Supp. 318 (N.D. GA. 1973) where a lender by holding a security interest in lots within a subdivision was held not to be a developer.

The Sixth Circuit in 1980 was presented with circumstances substantially similar to the case at bar, holding differently than the Fourth Circuit in its instant ruling. In Cumberland Capital Corp. v. Harris, 621 F.2d 246 (6th Cir. 1980), HUD contended Cumberland was a "developer" within the meaning and intent of ILSFDA. Cumberland argued otherwise.

Cumberland's involvement in land sales was an outgrowth of its activities as a lending institution. As security on loans, it took mortgages or deeds of trust on unimproved lots in a subdivision. On the default of a borrower, Cumberland would foreclose on the lot. At foreclosure, Cumberland would sometimes purchase the lot and thereafter offer it for resale.

It is in the **resale** of the lot by Cumberland that HUD took the position Cumberland was a developer and thus fell within the mandates of ILSFDA. The Appellate Court noted that Cumberland fell within the strict definition of the term "developer". Id. at 250. However, it found that for Cumberland to take title to a lot in subdivision from a person who was a lot

purchaser himself (and not the original developer), hold such lot for a period of time and thereafter advertise and sell such lot was not a develooper within the intents and purposes of the ILSFDA. In effect, the Court stated that to buy and resell a lot, and do no more, is insufficient to make it a developer.

The 1980 Cumberland case hinges on the concept of participation. The fact that Cumberland had taken title by deed in lieu of foreclosure or by foreclosure itself was immaterial; in effect acquisition of title is irrelevant. What is important is what does not occur after acquisition of title. Cumberland states that if the lot owner participates in the development of the subdivision, it is a developer and the ILSFDA applies; if no such participation occurs, then ILSFDA does not apply.

Significant also was the lack of any concern as to the number of lots involved. It was immaterial to the Sixth Circuit whether Cumberland owned one or more lots or how it acquired title. The ILSFDA will apply when a person sells "any lots" in a subdivision, be it one or more. Quantity, therefore, is not in issue in resolving who is and who is not a developer under the ILSFDA.

The Fourth Circuit also disregarded numerous state court decisions that had followed the McCown and Cumberland concepts which applied the definition of "developer" to different fact situations, mainly under condominium law. In McKnight v. Board of Directors, 512 N.E.2d 316 (Ohio 1987), the Ohio Supreme Court examined the definition of "developer" under the Ohio Condominium

Statute.[4] By applying the same ruling of Cumberland, the court held a mortgagee in acquiring title to a condominium and re-selling it does not of itself make the mortgagee a developer. However, becoming intertwined with the promotion and development of the complex and participating in and proffiting from the business results in the mortgagee becoming a developer. See also, Chotka v. Fidelco Growth Investors, 383 So.2 1169 (Fla. App. 1980) and First Federal Savings and Loan v. Department of Business Regulations, 472 So.2d 494 (Fla. App. 5 Dist. 1985).

CCMV in acquiring its 919 lots in the 4592 lot Subdivision had the Cumberland decision before it to act as a guide. Precedent having been established, CCMV in good faith believed itself not to be a developer because it simply acquired lots in a completed eight year old Subdivision, and marketed and resold them to the general public. During the holding period, CCMV took no participation in the Subdivision and performed absolutely nothing to any lot it owned. It followed the mandate and spirit of Cumberland exactly and was correct in concluding itself not to be a developer within the meaning of the ILSFDA.

For the Disrict Court and the Fourth Circuit to disregard the spirit and legislative intent of ILSFDA and to abrogate the line of cases in other Districts (as well as state court decisions) to the contrary results in the slimiest of minorities and a split which this Court must resolve. The

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[4] It should be noted that the definition of developer under the Ohio Condominium Statute parallels the definition of developer under the ILSFDA.

decision also represents a gross injustice in imposing joint and several liability of over eight million dollars on four individuals.

Statistics maintained by OILSR indicate that as of January 2, 1992, there had been 12,705 filings with HUD covering 6,579 subdivisions since the inception in April, 1969 of ILSFDA. There were 3,252 active registrations covering 2,056 subdivisions; 262 applicaitons were in process; and 9,453 filings had been suspended. The 6,579 subdivisions cover 6,121,410 lots with a total acreage of 5,490,012.

> In affirming the District Court, the Fourth Circuit has stated that if any one person sells or leases or offers to sell or leases or advertises for sale or lease any of these 6,121,410 lots that is not ocherwise exempted within these 6579 subdivisions, registration with HUD is mandatory giving rise to the need of a (I) Statement of Record (ii) mandatory language inclusion in the contract, and (iii) a right of recision notwithstanding that:
>
> - the seller is anyone other than the original developer;
> - the seller did no more than purchase a lot and attempted to re resell it;
> - the seller did not participate in any aspect of the subdivision's creation, construction, or sell-out;
> - the seller acquired one lot or multiple lots; or

- the seller acquired the lot by gift, devise, arms-length purchase, or otherwise.

This conclusion thwarts economic growth, frustrates the economy, and directly involves government in the affairs of buyer and seller of a lot in an otherwise completed subdivision. The District Court's ruling and the Fourth Circuit's affirmation disregard the essential grasp of the ILSFDA and has created a situation that prevents banks from lending on lots in a subdivision, enables current buyers to avoid a lot purchase where the predecessor in title failed to register with OILSR and has effectively placed the industry in a state of total paralysis.

B. Orders of civil restitution are not exempt from discharge pursuant to 11 U.S.C. § 523(a)(7).

In its Final Order of September 15, 1994, the District Court ordered each of the Individual Defendants, jointly and severally, to pay to HUD civil restitution amounting to $8,648,048.00, plus interest at the Treasury rate until paid. (A73-A76) In the accompanying Memorandum Opinion, the District Court ruled that this amount was exempt from bankruptcy discharge pursuant to 11 U.S.C. § 523(a)(7).(A66-A68) These rulings were affirmed by the Court of Appeals. These opinions are in direct conflict with the opinion of another jurisdiction on the same issue, In re Taite, 76 B.R. 764 (Bankr. C.D. Cal. 1987). The conflict arises out of a failure by the Fourth Circuit to interpret appropriately the scope of this Court's

ruling in Kelly v. Robinson, 479 U.S. 36 (1986), wherein this Court decided that orders of criminal restitution are automatically nondischargeable in bankruptcy.

This Court should grant certiorari in this case to resolve the emerging conflict of opinion and give needed guidance to the lower federal courts on the appropriate interpretation of this Court's prior holding in Kelly v. Robinson, as applied in civil cases.

In Kelly v. Robinson, 479 U.S. 36 (1986), this Court confronted the issue of whether criminal restitution orders were exempt from discharge pursuant to 11 U.S.C. § 523(a)(7). Even though the term "restitution" and the remedial doctrines it encompasses are not normally thought of in the same context as fines, penalties and forfeitures, the Court concluded that criminal restitution orders ought to be exempted under § 523(a)(7). The Court reasoned that even though one aspect of criminal restitution orders is to make the victim whole, the overriding interest at stake is to serve the punitive goals of the criminal justice system. Id. at 53. The Court was extremely wary of permitting the Bankruptcy Code to interfere with criminal sanctions, particularly against a historical background in which criminal orders had been immune from the bankruptcy process. Id. at 44-47.

None of these concerns come into play when the restitution order at issue results from a purely civil proceeding. In this case, the District Court ordered the Individual Defendants to pay restitution in an amount precisely equal to the court's

purported estimate of the value of the wrongdoing. It has been HUD's position throughout this litigation that the funds recovered would be held in trust for and disbursed to the lot purchasers. (A35) There can be no question that the overriding goal of the restitution at issue in this case is compensatory, and not punitive.

Even if civil restitution orders produce a deterrent effect upon the wrongdoer as a by-product, this does not change their essential nature as mechanisms by which victims are made whole. Deterrence and compensation go hand in hand in the civil law. But deterrence is not punishment. The goal of deterrence is advanced by compensatory remedies as well as punitive damages. Simply because the compensatory remedy causes a deterrent effect does not render that remedy punitive. Both compensatory and punitive remedies are designed to have deterrent effects. Accordingly, the presence of a deterrent effect or purpose in any given remedy does not indicate that the remedy is punitive.

Indeed, courts discussing the disgorgement remedy in the securities context have explicitly held that it is remedial in nature and not penal. S.E.C. v. Texas Gulf Sulphur Co., 446 F.2d 1301, 1308 (2d Cir. 1971), cert. denied, 404 U.S. 1005 (1971), S.E.C. v. Manor Nursing Centers, Inc., 458 F.2d 1082, 1104 (2d Cir. 1972). If the disgorgement ordered is sufficiently oppressive such that it constitutes a penalty, then it is unlawful. Id. This leads one to the inescapable conclusion that if the disgorgement ordered by the District Court below is a penalty, then it is unlawful

and must be dissolved. If, on the other hand, the relief ordered is remedial, then it is dischargeable. Either way, the District Court and Court of Appeals erred and must be reversed.

Punitive remedies are distinguished from compensatory remedies by the moral reprobation inherent in the former. Whereas the purposes of compensatory remedies are compensation and deterrence, the purposes of punitive remedies are retribution and deterrence. It is this sense of moral outrage, the retributive purpose, which distinguishes penal sanctions from compensatory remedies. The lack of a penal purpose to the order of civil restitution places it outside the realm of "fines, penalties and forfeitures."

The plain language of the statute compels this conclusion. The money judgment at issue is not a fine. Fines are not computed by reference to damage or loss, and then paid over to the victim. Restitution is. The judgment is not a penalty, for all the same reasons discussed above; its purpose is not punitive. Nor is it a forfeiture. Black's defines "forfeiture" as "something to which the right is lost by the commission of a crime or fault or the losing of something by way of penalty." This last term is also restricted to the domain of criminal or punitive sanctions. United States v. Bonanno Crime Family, 683 F. Supp. 1411, 1449 (E.D.N.Y. 1988)(disgorgement of lawful profits is impermissible forfeiture). Civil restitution obligations do not fall within the ambit of any of these three terms. Singularily and when read together, they

refer only to sanctions whose objective is overridingly penal in nature.

To date, there is only one court which has squarely addressed the question of dischargeability presented in this petition. It is factually on all fours with the case at bar, and analyzes and decides this very issue. The case is In re Taite, 76 B.R. 764 (Bankr. C.D. Cal. 1987), and was ignored by the Court of Appeals below.

The debtors in Taite were the principals of a defunct retail carpet business. Id. at 765-66. The corporation had been the subject of an investigation by the state Attorney General's office, which found evidence of widespread fraudulent activity. Id. A civil enforcement action was brought by the State of California against the individual debtors, which, after a three month trial, resulted in the imposition of civil penalties totaling $750,000.00 and an order of restitution in the amount of $256,645.00. Id. at 766, 768. The civil penalty was ordered pursuant to a statute which permitted the assessment of up to a $2,500 penalty for each violation. The restitution was calculated by receiving evidence of the aggregate losses of a pool of 3,001 defrauded customers. Id. at 768. The judgment was made payable to the state of California, but was to be used to reimburse former customers for funds paid to the debtors in fraudulent transactions. The debtors attempted to bankrupt both sums.

The court had little difficulty in concluding that the $750,000 civil penalty was nondischargeable pursuant to § 523(a)(7). The court analyzed the statute pursuant to which the penalties had been ordered, and cases interpreting the statute, and discerned

that the primary purpose of the civil penalties provision of the state Business and Professions Code was penal. Id. at 769. Sums awarded pursuant to that section were intended by the legislature to be punitive, rather than compensatory. Accordingly, the civil penalty was exempt from discharge. Id.

The opposite results with respect to the restitution award. The court acknowledged Kelly v. Robinson, but recognized that the reasoning and holding of that opinion was limited to criminal judgments. Id. In contrast, civil actions carry a lower standard of proof, and rarely require findings of criminal, wrongful intent as a prerequisite to liability. Even though the disgorgement of unlawful profits serve both compensatory and deterrent objectives, restitution/disgorgement awards are primarily intended to make whole the victims. Id. at 772.

Furthermore, the character of the party bringing the action ought not determine the dischargeability of the relief. Id. at 773. Had the individual customers brought action against the debtor seeking restitution for fraud, the judgment would not be automatically dischargeable as a fine owing to a governmental unit under § 523(a)(7). Rather, the customers would have to bring an adversary proceeding pursuant to § 523(c) to determine dischargeability under § 523(a)(2), the exemption from discharge for judgments predicated upon fraud. Id. The state ought not be able to deprive the debtors of their right to a hearing pursuant to § 523(c) simply by bringing the restitution action in the name of the state, rather than in the name of the customers, who are the true

beneficiaries of the recovery in either case. To hold otherwise would frustrate the overall bankruptcy goal of classifying claims, rather than creditors. Id.

All those compelling interests at stake in Robinson involving non-interference in the criminal sentencing process are absent in cases where only a civil money judgment is at stake. The bankruptcy court held the restitution award was not automatically immune from discharge pursuant to § 523(a)(7).

The single significant factual difference between Taite and the case at bar is that in Taite, the government agency plaintiff had brought a timely adversary proceeding in the bankruptcy court pursuant to § 523(c) to challenge dischargeability pursuant to the fraud exception of § 523(a)(2). Given the overwhelming evidence of fraud introduced at the debtors' three-month trial, the court had little difficulty in concluding that § 523(a)(2) exempted the judgment from discharge. By contrast, in the case at bar, HUD filed pleadings in the Bankruptcy Court for the Middle District of Pennsylvania, where the Defendants' bankruptcies were pending, requesting three extensions of time to file a dischargeability complaint. The bankruptcy court granted these requests, but HUD never followed through and brought the action. The Individual Defendants were subsequently discharged without adjudicating the issue.

Like the statute at issue in Taite, the ILSFDA also has a section which provides for civil penalties. 15 U.S.C. § 1717a permits the imposition of penalties in the amount of $1,000 per violation, if the defendant

knowingly violated the statute in a material way. This section may properly be characterized as penal, due to the burden of proving knowing intent and materiality. Furthermore, damages awarded pursuant to this section are computed per violation, without resort to any kind of actual damage calculation. Penalties awarded pursuant to this section would likely fall within the automatic exception of § 523(a)(7). By contrast, in the case at bar, HUD has requested relief pursuant to the general equity powers of the court, pursuant to 15 U.S.C. § 1719. Accordingly, the relief awarded by the District Court is no more than a regular civil money judgment. If HUD had wished to have its judgment exempt from discharge, it should have followed through with its previously expressed intentions and filed the requisite complaints in the bankruptcy court.

Congress intended to provide for penal sanctions for willful violations of the ILSFDA. It did so by enacting sections 1717 and 1717a of title 15. The former is a criminal statute authorizing incarceration. The latter is a civil statute which calculates penalties per violation, without regard to the quantum of the wrongdoing. The relief in this case was awarded pursuant to the general equitable grant of authority contained in § 1719. It is a compensatory money judgment, not a penal sanction. Penal sanctions may properly be classified as fines, penalties or forfeitures. Compensatory remedies may not. The judgment awarded by the District Court in the case at bar was compensatory in nature, not punitive. It is not exempt from discharge pursuant to §

523(a)(7), and is therefore a debt which is dischargeable and has been discharged in the Individual Defendants' bankruptcies.

C. The Courts below grossly misapplied the principles of restitutionary disgorgement in granting the relief ordered.

Pursuant to the general equitable grant of authority contained in the ILSFDA at 15 U.S.C. § 1719, the District Court ordered that the Individual Defendants disgorge $8.6 million in profits as restitution for the allegedly defrauded lot purchasers. The disgorgement remedy has its origins in securities fraud cases, Pidcock v. Sunnyland America, Inc., 854 F.2d 443, 446-47 (11th Cir. 1988), Litton Industries v. Lehman Bros., 734 F. Supp. 1071, 1074-76 (S.D.N.Y. 1990)(summarizing history and development of disgorgement remedy in securities cases), and is being applied in this case by analogy to the securities decisions. Kemp v. Peterson, 940 F.2d 110, 112 n. 1 (4th Cir. 1991).

1. The record contains no admissible evidence of damages.

When calculating damages in this action, the District Court proceeded upon the theory that CCMV bought lots for a low price, and then used sales practices allegedly prohibited by the ILSFDA to sell the lots at inflated prices. Kemp v. Cost Control Marketing and Management of Virginia, Inc., 790 F. Supp. 1275, 1278-79 (W.D. Va. 1992). It concluded that the amount it would order the defendants to disgorge would be the

difference between the fair market value of the lots and the amount for which the lots were subsequently sold. Id. This would equal CCMV's illegal profits. In order to fashion this remedy properly, HUD needed to furnish evidence of (1) the fair market value of all the lots, and (2) the amounts all of CCMV's customers paid for the lots. Rather than submitting admissible evidence of these facts, HUD instead filed the Henderson Declaration, a loose collection of hearsay gathered from survey responses to lot purchasers, which was then unthinkingly accepted by the District Court in its entirety over the Defendants' objections. (A98-A100)

Initially, the Henderson Declaration was not submitted by HUD for the purpose of finally calculating the amount of restitution. Rather, when the District Court was preparing to fashion its Interim Judgment Order, HUD requested that the Defendants be required to come up with an initial $100,000 contribution toward the lot purchasers' trust fund. Kemp 790 F. Supp. at 1278. HUD could only justify this amount if it could show that the Defendants' eventual liability, after all the evidence was in, would almost certainly exceed the requested initial payment of $100,000. Id. It then submitted the Henderson Declaration as evidence that the Defendants' eventual liability would most likely exceed $100,000. It was contemplated by all parties at this time that conclusive proof of damages would have to await further evidence.

In the Memorandum Opinion accompanying the Final Order of September 15, 1994, the District Court dispensed with the need to

take further evidence of damages by suddenly and without notice shifting the burden of proof to the Defendants. Cisneros v. CCMV, 862 F. Supp. 1531, 1534-35 (W.D. Va. 1994). It concluded that the approximation of damages contained in the Henderson Declaration would serve as the basis of the damages contained in the Final Order because the Defendants had failed to produce evidence to rebut it. Id. In doing so, the District Court improperly shifted the ultimate burden of proof on a material issue of fact to the Defendants. Furthermore, it did so without any notice to the Defendants, and in direct contravention of its Interim Judgment Order, which made explicit reference to HUD's burden to go forward with the evidence. Kemp v. Cost Control, 790 F. Supp at 1281-82.

As the sole authority for this burden-shifting tactic, HUD and the District and Fourth Circuit relied upon S.E.C. v. First City Financial Corp., 890 F.2d 1215 (D.C. Cir. 1989). If, as HUD asserts, First City stands for the proposition that the burden of proof with respect to all issues of damages may properly be shifted to the defendants in an administrative enforcement action, after the agency has proffered a modicum of hearsay on the issue, then it is poorly reasoned authority and should not be followed. As will be demonstrated, however, First City stands for no such thing.

At issue in First City was whether the defendants violated section 13(d) of the 1934 Securities and Exchange Act by failing to file a disclosure statement within the time required after acquiring over a five percent interest in the subject corporation. 890 F.2d at 1217. The District Court found that

the statute had been violated, and ordered the defendants to disgorge their illegal profits. Id. On appeal, the defendants challenged the District Court's measure of damages. Id. at 1230-31.

The S.E.C. and the District Court measured disgorgement as the total amount of the defendants' profit on the challenged transaction, which was the difference between the purchase price of the stock and the sale price of the stock. See, S.E.C. v. First City Financial Corp., 688 F. Supp. 705, 728 n. 24 (D.D.C. 1988). The defendants challenged this measure with the testimony of an expert, who purported to predict how much this total profit would have been diminished had the disclosure statement been timely filed. Id. at 727-28. Stated another way, the defendants contended that had they complied with the law, they still would have made money on the transaction, just not as much. Accordingly, the proper measure of damages, according to the defendants, is not the total profit on the illegal transaction, but only that amount of the profit which would not have been received but for the violation.

The appellate court recognized and accepted the proposition that any amounts ordered disgorged must be causally related to the fraud. 890 F.2d at 1231. However, it believed, as did the District Court, that the defendants' expert testimony, consisting of econometric predictions of stock market price responses to informational variables, was simply too speculative. Id. It was from this observation that sprung the statements relied upon by the Courts below in the case at bar. The First City court concluded that

since an actual measure of the precise amount of illegal profit is impossible, due to a plethora of uncertain variables, the measure of damages would have to be the total profit on the challenged transaction. Id. at 1232.

The distinction between First City and the instant case is a simple one. In First City, the defendants challenged not the quantum of evidence to support the court's findings, but the legal theory upon which the damage award was predicated. In the case at bar, the Defendants are challenging the District Court's interpretation of applicable law **and** the sufficiency of the evidence to uphold the damage award. The only evidence of damages in the record on this appeal is the multi-layered collection of inadmissible hearsay contained in the three-page Henderson Declaration. In First City, the District Court's summary of its factual finding took up twelve pages in the reporter volume, see, 688 F. Supp. at 708-19, and was drawn from transcripts of administrative hearings, pretrial depositions, and a trial transcript of over five hundred pages. Id. at 709 n. 2, 710 n. 3. In contrast to this appeal, the sufficiency of the evidence to support the District Court's factual findings was not at issue in First City.

Since it is impossible, as a practical matter (if not in theory), to distinguish between that portion of profit which is directly traceable to the violation, then the measure of damages can only be the total actual profit realized on the transactions. This is so because total actual profit can be precisely measured. The "illegal portion" of that profit cannot. Therefore, "the risk of uncertainty should fall on the wrongdoer

whose illegal conduct created that uncertainty." 890 F.2d at 1232.

In the words of Mark Batten, counsel for HUD below, the Henderson Declaration was only intended as an "initial guestimate" of damages to justify an initial interim disgorgement of $100,000. It should not have been admitted even for this limited purpose and was objected to by Defendants. The District Court compounded the gravity of this error, however, when it engaged in the unprecedented and impermissible shifting of the ultimate burden of proof of damages to the Defendants. As the burden of proof remained with HUD at all times, and it failed to introduce any admissible evidence on the issue, the District Court's calculation of damages, as affirmed by the Fourth Circuit, was error and must be reversed.

2. The record contains no evidence the Individual Defendants received any illegal profits.

The disgorgement remedy is only appropriate where the evidence indicates that those who are being ordered to disgorge illegal profits have in fact received illegal profits. The party seeking disgorgement has the burden of tracing the funds from the fraudulent transaction to the pocket of the party from whom disgorgement is sought. United States v. Bonanno Crime Family, 683 F. Supp. 1411, 1449 (E.D.N.Y. 1988). In order to support an award of disgorgement, the District Court must make detailed factual findings regarding the unlawful sources of the funds ordered disgorged. Schine Theatres

v. United States, 334 U.S. 110, 129 (1947). Otherwise, the relief would cease to be remedial, and would become an impermissible penalty. S.E.C. v. MacDonald, 699 F.2d 47, 54 (1st Cir. 1983), Zeller v. Bogue Electric Manufacturing Corp., 476 F.2d 795, 802 n. 10 (2d Cir. 1973), cert. denied, 414 U.S. 908 (1973), Restatement of Restitution § 150 (1937). If the relief ordered against each of the Individual Defendants is not limited by the amount of unlawful funds separately received by said Defendants, then it constitutes a penalty assessment and is unlawful. S.E.C. v. Texas Gulf Sulphur Co., 446 F.2d 1301, 1308 (2d Cir. 1971), cert. denied, 404 U.S. 1005 (1971), S.E.C. v. Manor Nursing Centers, Inc., 458 F.2d 1082, 1104 (2d Cir. 1972).

The cases cited demonstrate the principle that restitutionary disgorgement of profits is not always an available remedy in every case of fraud. It is only appropriate where the evidence shows that the defrauding party was left in possession of profits derived from the fraudulent transaction.

The District Court below at first acknowledged the validity of this proposition, then in the next breath completely ignored it. See, Kemp v. Cost Control, 790 F. Supp. at 1279-80. The District Court first stated, "[t]he court therefore may only recover from the individual defendants restitution in an amount that can be shown to be equal to the benefit they received from CCMV as a result of the violations of the Act." Then, in the paragraphs that follow, the District Court indulges itself in speculation and fantasy regarding what the evidence "may show" and

what "probably" happened, and what the "history of the case suggests" could have happened. Id. at 1279. The only specific fact cited is that one of the Individual Defendants gave his son a gift of $300,000, ***prior*** to the start of the instant litigation. No evidence as to the origin of the gift exists in this record. The District Court concluded, "The fact that the defendants could conduct their financial affairs with so little restraint ***suggests*** that before the commencement of this action the individual defendants received sizable profits from the violations." (emphasis added).

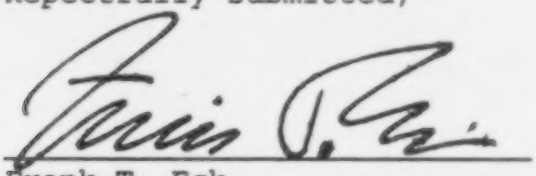
Even if one assumes that the Individual Defendants did "conduct their financial affairs with little restraint" prior to this litigation (and assume one must, for no evidence exists in this record), this merely establishes that before they were sued, the Individual Defendants lived comfortably. The assumption of wealth does nothing to establish the conclusion that the wealth was derived from any given source, be it inheritance, honest investments or unlawful activity. HUD utterly failed to satisfy its burden to prove that the Individual Defendants derived any profit from the allegedly illegal activities of CCMV, and the Courts below likewise failed to require the detailed factfinding necessitated by this Court's holding in Schine Theatres v. United States, 334 U.S. 110, 129 (1947).

X. CONCLUSION

Certiorari should be granted in this case to give further guidance to lower federal courts in the proper fashioning of

disgorgement remedies in the various contexts in which they arise, and to remedy the blatant disregard for this Court's precedent on the subject.

Repectfully submitted,



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Supreme Court, U.S.
FILED

No. 95-1233 JAN 31 1996

OFFICE OF THE CLERK

In The
Supreme Court of the United States

October Term 1995

COST CONTROL MARKETING & SALES MANAGEMENT OF VIRGINIA, INC.; WILLIAM P. PETERSON; ARTHUR KUJAWSKI; RICHARD R. COSTENBADER; JAMES M. MARLEY,
Petitioners,

v.

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT,
Respondent.

Petitioners' Appendix

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

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PUBLISHED
UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

U. S. DEPARTMENT OF HOUSING &
URBAN DEVELOPMENT,
Plaintiff-Appellee,

v.

COST CONTROL MARKETING & SALES
MANAGEMENT OF VIRGINIA,
INCORPORATED; WILLIAM P. PETERSON;
ARTHUR KUJAWSKI; RICHARD R.
COSTENBADER; JAMES M. MARLEY,
Defendants-Appellants,

and

THORNTON BYRON; STUART GUSKIND;
EARL HISSOM; MONTICELLO
DEVELOPMENT,
Defendants.

Appeal from the United States District Court
for the Western District of Virginia,
at Charlottesville.
James H. Michael Jr., District Judge.
(CA-89-4-C)

Argued: May 3, 1995
Decided: September 8, 1995
Entered: September 8, 1995

Before HALL and WILKINS, Circuit Judges, and
SPENCER, United States District Judge for the
Eastern District of Virginia,
sitting by designation.

Affirmed by published opinion. Judge Hall wrote the opinion, in which Judge Wilkins Judge Spencer joined.

COUNSEL

ARGUED: Francis Townley Eck, Brian Jay Grossman, ECK & COLLINS, Richmond, Virginia, for Appellants. Eric Johnson Mahr, Civil Division, UNITED STATES DEPARTMENT OF JUSTICE, Washington, D.C., for Appellee. **ON BRIEF:** Marshall E. Anders, ROSENBLUM & ANDERS, Stroudsburg, Pennsylvania, for Appellants. Frank W. Hunger, Assistant Attorney General, Robert P. Crouch, Jr., United States Attorney, William Kanter, Civil Division, UNITED STATES DEPARTMENT OF JUSTICE, Washington, D.C.; Peter S. Race, Audrey B. Kessner, UNITED STATES DEPARTMENT OF HOUSING & URBAN DEVELOPMENT, Washington, D.C., for Appellee.

OPINION

HALL, Circuit Judge:

Cost Control Marketing and Sales Management of Virginia, Inc., and four of its officers appeal orders of the district court enjoining them from violating the Interstate Land Sales Full Disclosure Act and ordering the officers to disgorge $8.65 million in profits to the Secretary of Housing and Urban Development. We affirm.

I

"Lake Monticello" is a large subdivision located in Fluvanna County, Virginia. It contains 4,592 lots, and was developed between 1968 and 1978 by Monticello Development Company. By 1978, all but 52 of the lots had been sold. Many of the sold lots remained unimproved, however.

In 1986, Cost Control Marketing & Sales management of Virginia, Inc., (CCMV) began purchasing unimproved lots at Lake Monticello. CCMV was formed for the sole purpose of buying and selling lots there. It is wholly owned by three of its officers-defendants William Peterson, Arthur Kujawski, and James Marley. Defendant Richard Costenbader is CCMV's chief executive officer.

By July, 1989, CCMV had purchased 919 vacant lots at the subdivision and had undertaken to aggressively advertise them in Washington, New York, and other northeastern markets. By December, 1989, CCMV had sold 585 of its lots. CCMV never took any steps to comply with the Interstate Land Sales Full Disclosure Act, 15 U.S.C. § 1701-1720(the Act). The Act requires "developers" and their agents to register with the Secretary of Housing and Urban Development (HUD), to provide specified disclosures to prospective purchasers, and to refrain from using certain sales practices. It is patterned, in purpose and in remedies, after the securities laws. Accordingly, in interpreting the Act, courts have applied the more comprehensively developed jurisprudence of securities cases. *Flint Ridge Development Co. v. Scenic Rivers Ass'n*, 426 U.S. 776, 777-778 (1976).

CCMV failed to register, failed to provide required property reports to purchasers, failed to inform purchaser of a two-year right to rescind afforded purchaser who had not been given the required reports, and flatly refused to rescind upon request. CCMV also used high-pressure, misleading marketing techniques. CCMV was able to sell lots at over three times their assessed value.

On November 15, 1989, HUD filed this suit in district court against CCMV, Costenbader, Peterson, Kujawski, and Marley.[1] HUD sought an injunction prohibiting further violations of the Act and disgorgement of all profits realized from CCMV's transactions at Lake Monticello. On February 14, 1990, the district court entered a preliminary injunction and froze the individuals defendants' assets (except for reasonable living expenses) to assure that they would not be dissipated. The individual defendants appealed.

This court affirmed the preliminary injunction but remanded for the district court to specifically state reasons why the asset freeze was necessary. *Kemp v. Peterson*, 940 F.2d 110 (4th Cir. 1991). In upholding the injunction, we rejected the defendants' only argument against liability-that CCMV is not a "developer" and the individual defendants are neither "developers" nor CCMV's "agents." *Id.* at 113.

On remand, HUD dropped its request for an asset freeze in connection with the preliminary injunction, though it still

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[1] Monticello Development Corp. and three of CCMV's salespersons were also sued, but the claims against them have been dismissed.

sought such relief as part of the final judgment. The district court granted summary judgment for HUD and entered an "interim" judgment order and memorandum opinion on April 22, 1992. *Kemp v. Cost Control Marketing and Sales Management of Virginia*, 790 F.Supp. 1275 (W.D.Va 1992).

In holding that a permanent injunction was necessary, the district court noted the "strong propensity" of the defendants to continue to engage in their violations unless enjoined. The court characterized the individual defendants as "absolutely unrepentant," noted that they had twice been certified in contempt by the magistrate, and concluded that "the individual defendants do not feel bound by the orders of this court (or by the law)." *Id.* at 1277.[2]

The court further held that disgorgement of the ill-gotten profits was an appropriate part of the equitable relief available to HUD. *Id.* at 1278. HUD requested that the individual defendants be ordered to make an initial payment of $100,000, and that they be made jointly and severally liable for whatever final figure the court determined after further proceedings.

In support of its request for the interim payment, HUD presented the declaration of the director of its Interstate Land Sales Registration Division, Roger Henderson. Henderson stated that a sample of

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[2] Because it believed that an additional sanction would serve no purpose, HUD dropped its request that the district court act on the magistrate's two certifications of contempt. The district court acceded, but stated on the record, "I want no doubt in anyone's mind that on that record made before the magistrate judge, these individual defendants are flatly guilty of contempt of court."

258 lots[3] sold by CCMV at Lake Monticello revealed an average disparity of $18,558 between the sale price and assessed value.[4] Henderson then multiplied this disparity times the 466 lots HUD could then show CCMV had sold, and arrived at an approximate profit of about $8.65 million. In light of this substantial figure, which, inasmuch as CCMV admits selling 585 lots, may have been lower than the true amount, the district court had no problem ordering $100,000 as an interim judgment. Finally, in light of the defendants' recalcitrance and unrepentance, "and the strong evidence...that the individual defendants cannot be trusted to conserve their assets[,]"[5] the court reinstated the asset freeze. *Id.* at 1281-1282.

The defendants noted an interlocutory appeal, which this court dismissed. *HUD v. Peterson*, No. 92-1570 (4th Cir. June 19, 1992). Marley, Peterson, and Costenbader (but not Kujawski) then filed voluntary Chapter 7 bankruptcy petitions in the bankruptcy court for Middle District of Pennsylvania. They received discharges in January, 1993.

Because HUD believed that neither the automatic stay nor the bankruptcy discharge applied to this case, it proceeded with

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[3] HUD mailed questionnaires to 466 lot purchasers it had identified. The 258 questionnaires returned formed its sample.

[4] By law, Virginia assesses at 100% of market value. Though the defendants suggest that assessments are *de facto* below market value, they presented no evidence of it.

[5] As "but one egregious example" of the defendants' profligate dissipation of assets, the court cited a "purported gift" of $300,000 from defendant Marley to his son. 790 F.Supp. at 1279-1280.

attempts at discovery aimed at assisting in a final calculation of disgorgement of profits. The defendants refused to answer interrogatories and failed to make the initial $100,000 payment required by the interim judgment order. The district court issued a rule to show cause, and only one (Kujawski) of the defendants even bothered to respond to it.

On January 7, 1994, HUD filed a motion for entry of final judgment based on the individual defendants' failure to produce evidence to rebut the reasonable approximation of profits contained in the Henderson declaration. The magistrate recommended granting final judgment. The defendants objected to the report, but the district court adopted the recommended disposition in a memorandum opinion. *Cisneros v. Cost Control Marketing and Sales Management of Virginia*, 862 F.Supp. 1531 (W.D.Va. 1994). The final judgment makes the individual defendants jointly and severally liable for $8.65 million, payable to HUD.

CCMV and the individual defendants appeal.[6]

II

The defendants persist in arguing that CCMV is not a "developer" because it simply bought lots that had been developed by someone else. If the dictionary definition of "developer" controlled, they might have a

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[6] Though it was clearly intended to resolve all claims against all parties, the final disgorgement order does not mention **CCMV** by name. **HUD** has not sought correction of this inadvertent error, and it states in its brief that it is content to seek satisfaction of its judgment from the four individual defendants.

fair case. But the Act defines "developer" in a manner that clearly includes CCMV:

> any person who, directly or indirectly, sells or leases, or offers to sell or lease, or advertises for sale or lease any lots in a subdivision.

15 U.S.C. §1701(5). This court rejected CCMV's argument in upholding the temporary injunction, and in a subsequent case, we flatly held that "developer" is not limited, as the defendants continue to argue, to just the initial entity that subdivided and platted the land. *Olsen v. Lake Country, Inc.*, 955 F.2d 203, 205-206 (4th Cir. 1991), *cert. denied*, 503 U.S. 972 (1992). CCMV was a defendant in *Olsen*-though not the primary defendant-and the same Richmond law firm represented the "developer" there. 955 F.2d at 204 and *id.* n.1. Consequently, the defendants' failure to cite *Olsen* in its brief or to respond to HUD's citation in its reply are troubling to the court, to say the least. We remind counsel that a lawyer's duty of candor to the court must always prevail in any conflict with the duty of zealous advocacy.

In any event, CCMV is a developer under circuit precedent, the law of the case, and the plain language of the statute.

III

The individual defendants' assertion that they are not "developers" or "agents" of CCMV is also foreclosed by the law of the case. *See Kemp*, 940 F.2d at 113.

IV

When the interim judgment order was entered, HUD and the district court doubtless envisioned that a searching inquiry into the individual defendants' finances would follow to see how much of the ill-gotten gains had flowed through CCMV and into their pockets. The district court's order clearly contemplated the submission of much more evidence.

It never happened. The defendants refused to answer interrogatories or produce documents that might have led to a more exact figure than the $8.65 million estimated in the Henderson declaration, notwithstanding certifications of contempt. Only one of the four bothered to respond to an order to show cause. Likewise, during the 27 months between the entry of the interim judgment and the final judgment, the defendants produced no evidence of their own to contradict the Henderson declaration, though, if its calculation were inflated, they had every incentive to do so.[7]

The defendants nonetheless have the chutzpah to attack the sufficiency of HUD's proof to support the $8.65 million award. Though the district court considered but chose not to enter judgment as a sanction, we think that the defendants' discovery

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[7] No skeptic can ignore the corollary inference-production of evidence may well have shown that Henderson underestimated the defendants' ill-gotten gains. As we noted above, CCMV sold over 25% more lots than Henderson supposed. Moreover, a Lake Monticello homeowners' association newsletter suggests that CCMV may have purchased lots at well below their assessed value.

misconduct alone might be sufficient to uphold the award.

In any event, HUD's evidence is absolutely uncontradicted. The defendants argue simply that the Henderson declaration is hearsay and therefore of no value whatever on summary judgment. This argument is their best; hearsay like other evidence inadmissible at trial is ordinarily an inadequate basis for summary judgment. Maryland Highways Contractors Ass'n v. State of Maryland, 933 F.2d 1246, 1251-1252 (4th Cir.), cert. denied, 502 U.S. 939 (1991).[8]

Here, the Henderson declaration serves as a summary of voluminous evidence. Something like it would doubtless have been permitted at a trial of this case. See Fed. R. Evid. 1006. Moreover, though the parties do not emphasize the pint in the briefs, there are sworn declarations from eleven or the lot purchasers in the record. The sales figures and assessed values sworn to by these declarations[9] corroborate the Henderson

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[8] This rule is not unfailingly rigid, though. In *Celotex Corp. v. Catrett*, 477 U.S. 317, 327 (1986), the Supreme Court held that the nonmoving party could defeat summary judgment with materials capable of being reduced to admissible evidence at trial. HUD, of course, was the moving party; nonetheless, the practical question presented by a motion for summary judgment is whether the case presents a genuine issue of fact for trial rather than whether the parties have put their evidence in final form.

[9] The eleven owners purchased a total of twelve unimproved lots at prices ranging from $20,900 to $33,200. Three of the eleven provided copies of their latest tax assessments; two of these lots were assessed at $7,000 and the other at $7,500. The purchase prices are of course based on the purchasers' personal knowledge, and the tax assessments are admissible under Fed. R. Evid. 803(8).

declaration's calculation. In addition, Bobby C. Durham, a real estate agent in Charlottesville, Virginia, sponsored a copy of the local Multiple-Listing Service (MLS) printout for mid November, 1989. The MLS information showed that dozens of unimproved lots at Lake Monticello had sold for less than $10,000 during early and mid-1989, and dozens more were listed for sale at similar prices as of November 14, 1989.[10] We believe that this admissible evidence serves as a sufficient foundation for the Henderson declaration, especially under the peculiar facts of this case, in which the defendants have contumaciously refused to disclose evidence that would have provided a better foundation.

Finally, the district court noted that estimating ill-gotten profits to fashion a disgorgement remedy is an imprecise science, and it adopted the analysis of the D.C. Circuit in *SEC v. First City Financial Corp.*, 890 F.2d 1215 (D.C. Cir. 1989). Though the government always retains the burden of persuasion, *First City* and the district court set a practical standard for the government's initial burden of coming forward. Once the government establishes the defendants' liability ad produces a reasonable approximation of the illegal profits, it is up to the wrongdoers to come forward with evidence to rebut the approximation. Requiring too detailed an initial showing by

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[10] The **MLS** printout qualifies as a "record [] of regularly conducted activity" under Fed. R. Evid. 803(6). Though Durham was not the custodian of the **MLS** records, Rule 803(6) permits such records to be sponsored by any "qualified witness, unless the source of the information or circumstanc s of preparation indicate lack of trustworthiness."

the government could provide a sanctuary for defendants, like these, who are wily or obstinate enough to hide the truth.

HUD's disgorgement calculation may be based on thin evidence, but it prevails over the defendants' evidence, which is nil.

V.

In the first appeal in this case, this court held that an asset freeze, though extraordinary, is within the district court's power in fashioning an equitable remedy. "Such a remedy...must be supported by a showing of fraud, mismanagement, or other reason to believe that, absent the freeze order, the assets would be depleted or otherwise become unavailable." *Kemp*, 940 F.2d at 114. The court remanded only because it was unable to discern the district court's specific reasons for entering the freeze. Fed.R.Civ.P.65(d).

The district court made no such error of omission here. It stated flatly, after an opinion teeming with references to the defendants' recalcitrance, that "the individual defendants cannot be trusted to conserve their assets."

VI.

The three individual defendants who filed bankruptcy petitions argue that they should not be faulted for failing to defend this action during the bankruptcy proceeding and that their discharge should bar entry of the disgorgement order.

Though the discharge issue is reasonable close, we affirm for the reasons given by the

district court. 862 F.Supp. at 1533-1534.[11] In short, though the filing of a bankruptcy petition ordinarily acts as a stay of pending judicial proceedings, 11 U.S.C. §362(a)(1), the stay does not apply to "the commencement or continuation of an action or proceeding by a governmental unit to enforce such governmental unit's police or regulatory power[.]"§362(b)(4). This exception to the stay precisely fits this case.[12] *See Board of Governors of Federal Reserve System v. Mcorp Financial*, 502 U.S. 32, 39-40 (1991).

Moreover, because discharge in bankruptcy is not intended to be a haven for wrongdoers, a Chapter 7 debtor may not discharge "a fine, penalty, or forfeiture payable to and for the benefit of a governmental unit, and [that] is not compensation for actual pecuniary loss[.]" 11 U.S.C. §523(a)(7). The defendants have a fair argument here, because HUD has measured its disgorgement remedy by the amount lot purchasers lost, and it has often stated in this record that it intends to use some or all of its recovery to reimburse those purchasers. On the other hand, the final judgment orders payment to HUD and imposes no obligation on HUD to disburse the money to anyone.

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[11] The district court had concurrent jurisdiction with the bankruptcy court to determine the affect of the bankruptcy proceeding on this case, *Brock v. Morysville Body Works, Inc.*, 829 F.2d 383 (3rd Cir. 1987), and, because the district court's jurisdiction attached first in time, it was superior. *Kline v. Burke Construction Co.*, 260 U.S. 226 (1922).

[12] The stay, moreover, terminates by operation of law upon entry of the discharge. 11 U.S.C. §362(c)(2)(C).

The Supreme Court has give §523(a)(7) a broad reading, and has held that it applies to all criminal and civil penalties, even those designed to provide restitution to injured private citizens. *Kelly v. Robinson*, 479 U.S. 36 (1986) (criminal restitution obligation was not dischargeable); *Pennsylvania Dep't of Public welfare v. Davenport*, 495 U.S. 552, 562 (1990) (stating that §523(a)(7) applies to both criminal and civil fines).

We interpret these cases to say that so long as the government's interest in enforcing a debt it *penal*, it makes no difference that injured person may thereby receive compensation for pecuniary loss. In other words, the "not compensation for actual pecuniary loss" phrase in §523(a)(7) refers to the *government's* pecuniary loss.[13] For example, a person drives recklessly and collides with a city garbage truck. A city policeman issues him a traffic ticket, and the city attorney files a negligence suit and obtains a judgment for the amount of damage to the garbage truck. The person can discharge the judgment for damaging the truck, but he cannot discharge his reckless driving fine. We therefore agree with the district court that the judgment in this case is not dischargeable in a Chapter 7 bankruptcy proceeding.

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[13] Even where a debt is intended to help defray the expense of government, it may not be dischargeable if its primary purpose is penal. *E.g.*, *In re Thompson*, 16 F.3d 576 (4th Cir. 1994) (court costs assessed against convicted criminals defendant were not dischargeable).

The judgment is affirmed

AFFIRMED

IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF VIRGINIA
CHARLOTTESVILLE DIVISION

JACK KEMP, SECRETARY OF THE DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT,

Plaintiff

v.

COST CONTROL MARKETING AND MANAGEMENT OF VIRGINIA, INC., et. al.,

Defendants

Civil Action No. 89-0042-C

Entered February 14, 1990

O R D E R

Honorable James H. Michael, Jr.

Upon consideration of the motion of plaintiff Jack Kemp, Secretary of the Department of Housing and Urban Development, for a preliminary injunction, defendants' reposes thereto, and the entire record herein, and a hearing having been held on December 22, 1989, it is this day

ADJUDGE AND ORDERED

as follows:

1. The Motion of plaintiff for a preliminary injunction shall be, and it hereby is, granted. The court finds on the record now before it that defendant Cost control Marketing and Sales Management of Virginia, Inc. (CCMV) is a developer within the meaning of the Interstate Land Sales Full Disclosure Act (the Act), 15 U.S.C. §

1701(5). As there is no dispute in the evidence before the court at this juncture, it follows that pursuant to 15 U.S.C. § 1714, defendants CCMV, William Peterson, Arthur Kujawski, James Marley, Richard Costenbader, Thornton Byron, Stuart Guskind, and Earl Hissom have failed to comply with the requirements of the Act and, unless preliminary enjoined, there is a reasonable likelihood such conduct will continue. The court also finds that the ancillary relief requested by plaintiff is appropriate to secure and maintain adequate assets to respond to any ultimate determination of liability.

2. CCMV, its officers, agents, and employees, including but not limited to defendants Peterson, Kujawski, Marley, Costenbader, Byron, Guskind, and Hissom, as well as all individuals and entities acting in concert or participation with any defendant, are enjoined from violating the Act and its implementing rules and regulations including, but not limited to: (a) advertising, offering to sell, or selling lots in the Lake Monticello subdivision, Fluavanna County, Virginia, while there is no Statement of Record of Property Report in effect with respect to the subdivision pursuant to 15 U.S.C. § 1704-1707; (b) failing to provide purchasers with Property Reports prior to the signing of their lot sales contract as required by 15 U.S.C. § 1703(a)(1)(B); or (c) using sales contracts or agreements, including promissory notes, that do not set forth purchasers' revocation rights, as required by 15 U.S.C. § 1703(b) & (c).

3. Plaintiff, by counsel, having agreed in open court, both before this court and before Magistrate Crigler, that HUD forthwith and expeditiously will process and respond to any application for registration or exemption of CCMV or any of the defendants under the Act, plaintiff hereby is directed so to process any and all applications filed by any such party for registration or exemption of the subject conduct under the Act.

4. Defendants CCMV, Peterson, Marley, Kujawski, Costenbader, and all individuals or entities acting in concert or participation with them are enjoined from transferring or disposing of those defendants' corporate or personal monies or other assets, except for payment of reasonable living expenses and expenses incurred in the normal course of business, until this action is finally adjudicated. The court hereby refers this action to Magistrate B. Waugh Crigler, pursuant to 28 U.S.C. §§ 636 (b)(1)(A) and 636 (b)(2), to review and take action with respect to the propriety of any payment, disbursement or transfer of assets that is challenged by plaintiff as being beyond the scope of reasonable living expenses or normal business expenses. Defendants CCMV, Peterson, Marley, Kujawski, and Costenbader shall each report all assets and also all payments, disbursements, and transfers made for reasonable living expenses or normal business expenses, listing the amount of each expenditure or transfer, the purpose of each expenditure or transfer, and the payee or transferee. Defendant CCMV shall submit such reports on a biweekly basis, and all other individual defendants shall submit such reports on a monthly basis, and shall include

all such information mentioned above commencing December 22, 1989. The form such reports shall take shall be fixed by the Magistrate.

5. Defendants CCMV, Peterson, Marley, Kujawski, Costenbader, and all individuals or entities acting in concert or participation with them are enjoined from assigning or transferring the right to receive payments arising from past or future sale of lots in the Lake Monticello subdivision to any individual or entity other than a currently-established creditor of CCMV, such as Northeastern Bank of Pennsylvania, pending further Order of the Court or final adjudication of this action. However, defendants CCMV, Peterson, Marely, Kujawski, Costenbader, and all individuals or entities acting in concert or participation with them are specifically enjoined from making any such assignment or transfer, except with leave of this court or of the Magistrate, to themselves or their families, to Cost Control Marketing and Sales Management, Inc. (a Pennsylvania corporation), or to any other entity wholly or partially owned by defendants, their families, employees or agents, even if such assignee or transferee is a currently-established creditor of CCMV.

6. All monies received by defendants CCMV, Peterson, Kujawski, Marley, and Costenbader on or after the date of this Order from the sale of lots at Lake Monticello shall be placed by defendant in a separate interest-bearing account with a federally-chartered financial institution within this judicial district pending final disposition of this case. Funds deposited in this account shall be available only to meet

the ordinary and normal business expenses of CCMV. Magistrate Crigler shall review and take action with respect to the propriety of any payment, disbursement or transfer of such funds that is challenged by plaintiff as being beyond the scope of ordinary and normal business expenses. Defendants shall report all amount placed in the account and any withdrawals or transfers of funds from the account that are made to pay CCMV's ordinary and normal business expenses, listing the amount of each deposit, withdrawal or transfer, the purpose of each expenditure or transfer and the payee or transferee. Such reports shall take the form prescribed by the Magistrate. Defendants shall submit such reports to Magistrate Crigler and the parties herein in the form and commencing as set forth above. A copy of the most recent account statement from the financial institution, reflecting all deposits, withdrawals and transfers, shall be attached to each report.

7. All objections to any biweekly or monthly report shall be filed by plaintiff within 14 days of the date copies thereof are certified as filed; provided, however, plaintiff shall not be deemed to have waived his right to object to the contents of any report should the grounds for any objection become known to him or his agents after the period for objection has elapsed. Defendants shall cause copies of all reports to be certified for filing and delivered to counsel for plaintiff by overnight mail.

8. All reports filed pursuant hereto shall be held in confidence and neither the whole contents thereof nor any part thereof may be published or otherwise disclosed

expect and unless plaintiff files objection to any report or upon order of this court or the Magistrate. All objections shall be hear under such conditions as the Magistrate may direct.

The provisions of this Order shall remain in effect pending a final ruling and entry of judgment in this action.

The Clerk is hereby directed to send a certified copy of this Order to all counsel of record and to Magistrate B. Waugh Crigler.

DATED: This 14th day of February, 1990.

/s/ James H. Michael Jr.
James H. Michael, Jr.
United States District Judge

940 F.2d 110, Kemp v. Peterson, (C.A. 4(Va.)1991)
20 Fed.R.Serv.3d 1088

Jack KEMP, Secretary of Housing and Urban Development, Plaintiff-Appellee
v.
William P. PETERSON; Arthur Kujawski; Richard R. Costenbader; James M. Marley, Defendants-Appellants, and
Cost Control Marketing & Sales Management of Virginia, Incorporated; Thornton Byron; Stuart Guskind; Earl Hissom; Monticello Development, Defendants.

No. 90-2049
United States Court of Appeals
Fourth Circuit
Argued Dec. 4, 1990.
Decided Aug. 2, 1991.
Entered Aug. 2, 1991.

*111 Marshall E. Anders, Rosenblum & Anders, P.C., Stoudsburg, Pa., for defendants-appellants.

Margaret Susan Hewing, Civ. Div., U.S. Dept. of Justice, Washington D.C., argued (Stuart M. Gerson, Asst. Atty. Gen., Barbara Biddle, Civ. Div., U.S. Dept. of Justice, Washington D.C., John P. Alderman, U.S. Atty., Roanoke, Va., on the brief), for plaintiff-appellee.

*112 Before SPROUSE, Circuit Judge, CHAPMAN, Senior Circuit Judge, and MERHIGE, Senior District Judge for the Eastern District Virginia, sitting by designation.

OPINION

SPROUSE, Circuit Judge:

William Peterson, Arthur Kujawski, James Marley, and Richard Costenbader, officers and owners of Cost Control Marketing & Sales Management of Virginia, Inc. ("CCMV"), appeal from the order of the district court enjoining them from future violations of the Interstate Land Sales Full Disclosure Act, 15 *U.S.C. Sec. 1701* et seq., and freezing their individual assets as security for putative claims of lot owners. We affirm the injunction, but remand to the district court for factual findings concerning the freeze order pursuant to Rule 65(d) of the Federal Rules of Civil Procedure.

I.

CCMV is a corporation wholly-owned by its officers, established for the sole purpose of selling lots of land in Lake Monticello, a property subdivision located in Fluvanna County, Virginia. The subdivision is comprised of 4,592 lots. At the commencement of this suit, CCMV had acquired 918 lots--150 lots form the original developer of the land and 768 from individual sellers. CCMV's sellers are not parties to this suit. Of the 918 lots, CCMV resold 502 to individual purchasers, leaving it with 416 remaining lots.

The Interstate Land Sales Full Disclosure Act (the "Act") requires developers of land to register with the Secretary of the Department of Housing and

Urban Development ("the Secretary") and to make disclosures to potential purchasers of lots within a subdivision. The Act is designed to prevent fraud and deception in the sale of undeveloped land. (*FN1*) The Secretary filed a complaint and motion for Preliminary Injunction against CCMV. It charged CCMV with violating the registration and disclosure provisions of the Act, as well as certain other prohibited sales practices, including overcharging for closing costs, misleading advertising, and misinforming purchasers that they had no rights to revoke their contracts.

Following a hearing on the motion, the district court ordered a preliminary injunction, enjoining future violations of the Act and freezing the corporate and individual assets of the officers. In addition, it ordered future proceeds from the sale of lots placed in an escrow account pending an ultimate determination on the issue of liability. Finally, it ordered the defendants to submit biweekly or monthly reports to a magistrate judge, to account for personal and business expenses. The officers do not appeal from the injunction, *(FN2)* only the order freezing their assets and requiring them to submit monthly accounting reports to monitor compliance. Although we affirm the injunction ruling, including the monthly accounting order, we remand the case in order for the district court to make the appropriate factual findings under Fed.R.Civ.P. 65(d) *(FN3)* with respect to the freezing of assets.

II

There is no question that the district court was within its authority in enjoining *113 the corporate and individual defendants from future violations of the Act. 15 *U.S.C. Sec. 1714(a). (FN4)* Since the court determined that the Secretary met his burden of showing violations of the Act (failure to register and make the required disclosures), as well as a "reasonable likelihood" of continued violations, there was no abuse of discretion with regard to this part of the district court's order. See *SEC v. Management Dynamics, Inc., 515 F.2d 801, 808-809* (2d cir. 1975) (once plaintiffs show a violation of a specific federal statute, the usual balancing of equities is not required prior to enjoining future violations.

[1] Although appellants do not contest the authority of the district court to grant an injunction in the appropriate circumstances, they object to the monthly accounting requirement and freeze order as it pertains to them. First, they argue that the accounting order is burdensome and impermissibly intrusive. Second, they argue that since they are neither developers nor agents, they are not required to comply with the requirements of the Act, nor can they be held individually liable for the corporation's violations. We find their arguments unpersuasive.

[2] Appellants' principal objection to the monthly accounting order concerns the prerogative given to the Secretary to object to each accounting report submitted. In our view, this objection falls within the general

rule that a court is authorized to issue all order necessary to enforce orders it has previously issued in the exercise of its jurisdiction. *28 U.S.C. Sec. 1651(a) ("All Writs Act"); United States v. New York Tel. Co., 434 U.S. 159, 172, 98 S.Ct. 364, 372, 54 L.Ed.2d 376 (1977); National Org. for the Reform of Marijuana Laws v. Mullen, 828 F.2d 536, 544 (9th Cir. 1987).* We find no abuse of discretion, since the order bears a direct relationship to the district court's purpose of monitoring compliance with the freeze order.

[3] Appellants' contention that they are not individually responsible for violations of the Act and , therefore, should not be subject to a freeze of their personal assets, is also without merit. The Act defines "developer" as "any person who, directly or indirectly, sells or leases, or offers to sell or lease, or advertises for sale or lease any lots in a subdivision..." *15 U.S.C. Sec. 1701(5).* "Agent" is defined as "any person who represents, or acts for or on behalf of, a developer in selling or leasing, or offering to sell or lease, any lot or lots in a subdivision." *15 U.S.C. Sec. 1701(6).* The district court held that CCMV fell within the language of the statute. Moreover, officers, directors, and participating planners may be held individually liable for violations of the Act, notwithstanding the absence of a clause in the Act establishing liability for "controlling stockholders, officers and directors." *McCown v. Heidler, 527 F.2d 204, 207 (10th Cir. 1975)* (quoting *Adolphus v. Zebelman, 486 F.2d 1323, 1325 (8th Cir. 1973).* To hold otherwise would defeat the purpose of the Act, since it is

the officers of the corporation who are behind the alleged fraud. See also *SEC v. First Am. Bank & Trust Co., 481 F.2d 673 (8th Cir. 1973).*

III.

[4] Once having found that appellants may be held individually liable, we turn to the issue of whether the district court abused its discretion in freezing appellants' individual assets and requiring that money received from the sale of lots at Lake Monticello be placed in escrow. Initially, we note that since the district court's order was preliminary in nature, pending a final determination of liability, the freezing of funds and the escrowing of monies received from the sale of land may be proper without respect to whether those monies are traceable proceeds or profits and *114 income from the proceeds. The purpose of a preliminary injunction is to preserve the status quo "where the balance of hardships tips decidedly toward the party requesting the temporary relief and that party has raised questions going to the merits so serious, substantial, and difficult as to make them a fair ground for litigation..." *International Controls Corp. v. Vesco, 490 F.2d 1334 (2d Cir.)* (citations omitted), cert. denied, *417 U.S. 932, 94 S.Ct. 2644, 41 L.Ed.2d 236 (1974).* If it can be shown that such a purpose would be served by the enforcement of the district court's order, it should be affirmed. The cases cited by appellants in arguing that profits and income from proceeds may not be disgorged are inapposite in that they profit actual disgorgement in situations where liability has been established. *SEC v.*

Manor Nursing Centers, Inc., 458 F.2d 1082 (2d Cir. 1972); *SEC v. Blavin, 760 F.2d 706, 713* (6th Cir. 1985).

[5] Equity powers conferred by the Act permit the court to fashion appropriate remedies. *15 U.S.C. Sec. 1719.* See Also *Manor Nursing Centers, 458 F.2d at 1103* (parallel provision in Securities Act confers equity jurisdiction authorizing order to disgorge proceeds received from violations of that Act). Although "freezing" is an extraordinary remedy, there is no question as to the general authority of the court to fashion the remedy as it did. See *Vesco*, 490 F.2d at 1347; see also *SEC v. American Bd. of Trades, Inc.*, 830 F.2d 431, 438 (2d) Cir. 1987), cert. denied, 485 U.S. 938, 108 S.Ct. 1118, 99 L.Ed.2d 278 (1988). Such a remedy, of course, must be supported by a showing of fraud, mismanagement, or other reason to believe that, absent the freeze order, the assets would be depleted or otherwise become unavailable. See *American Bd. of Trade*, 830 F.2d at 438-39; Bowler, 427 F.2d 190, 197 (4th Cir. 1970).

[6] In order to determine if the freeze order was properly based on such showing, however, we must be able to discern the trial court's reasoning. Fed.R.Civ.P. 65(d); see also *United States, Dep't of the Air Force v. Carolina Parachute Corp.*, 907 F.2d 1469, 1475 (4th Cir. 1990). Here, the district court failed to make factual findings or state reasons for issuing the order. We, therefore, remand to provide it that opportunity. See *FDIC v. Jones*, 846 F.2d 221, 240 (4th Cir. 1988). In view of the above, the judgment of the district court is affirmed in part, and

remanded for further action consistent with this opinion.

AFFIRMED IN PART AND REMANDED.

FN1. In its philosophy and provisions for disclosure, the Act closely resembles the Securities Act of 1933, 15 U.S.C. Sec. 77a et seq. Therefore, cases interpreting the Securities Act are instructive. See *Flint Ridge Dev. Co. v. Scenic Rivers Asoc.*, 426 U.S. 776, 778, 96 S.Ct. 2430, 2433-34, 49 L.Ed.2d 205(1976).

FN2. The officers filed a motion for clarification of the district court's order, which was referred to a magistrate judge. In their motion, defendants took issue with the district court's conclusion that CCMV is a "developer" within the meaning of the Act. The magistrate judge recommended minor changes, including a clarification in the order that the ruling as to whether CCMV was a "developer" was only based on the record before the court at the time it was issued.

FN3. Rule 65(d) states: "Every order granting an injunction and every restraining order shall set forth the reasons for its issuance; shall be specific in terms; shall describe in reasonable detail, and not by reference to the complaint or other document, the act or acts sought to be restrained..."

FN4. *15 U.S.C. Sec.* 1714(a) provides in relevant part:

Whenever it shall appear to the Secretary that any person is engaged or about to

engage in any acts or practices which constitute or will constitute a violation of the provisions of this chapter, or of any rule or regulation prescribed pursuant thereto, he may, in his discretion, bring an actin in any district court... to enjoin such acts or practices, and, upon a proper showing, a permanent or temporary injunction or restraining order shall be granted without bond...

IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF VIRGINIA
CHARLOTTESVILLE DIVISION

JACK KEMP, SECRETARY OF THE
DEPARTMENT OF HOUSING AND
URBAN DEVELOPMENT,

Plaintiff

v.

COST CONTROL MARKETING AND
SALES MANAGEMENT OF VIRGINIA,
INC., et al.,

Defendants

Civil Action No. 89-0042-C

Entered April 22, 1992

MEMORANDUM OPINION

JUDGE JAMES H. MICHAEL, JR.

This civil action was brought by the United States Department of Housing and Urban Development ("HUD") against Cost Control Marketing and Sales Management of Virginia ("CCMV") and several of its officers and sales agents ("the individual defendants')to enforce the Interstate Land Sales Full Disclosure Act ("the Act") 15 U.S.C. § 1701 et seq. (1982). Summary judgment has been granted against the individual defendants for violating the registration and disclosure requirements of the Act, and the so-called "anti-fraud" provisions of the Act. The

court must now craft an interim judgment order.

The facts in this case are no longer in dispute. CCMV is a Virginia corporation engaged in the purchase, marketing, and sale of lots of land at Lake Monticello, in Fluvanna County, Virginia. HUD filed this action against CCMV, and the individual defendants William Peterson, President of CCMV; Arthur Kujawski, Vice President of CCMV; Richard Costenbader, Chief Executive Officer of CCMV; James Marley, Secretary and Treasurer of CCMV; and Thornton Byron, a sales agent of CCMV. All of the defendants are "developers" as that word is defined at 15 U.S.C. § 1701(5). See Kemp v. Peterson, 940 F.2d 110, 113 (4th Cir. 1991). Their activities therefore came within the purview of the Act.

The complaint alleged and this court found on a motion for partial summary judgment as to Counts I and II of the Complaint, that as of January 1, 1987, CCMV and the individual defendants had violated the "sales practices" requirements of the Act by selling lots without filing a statement of record with HUD's Office of Interstate Land Sales, see 15 U.S.C. §1703(a)(1)(A), and without providing purchasers with statutorily required property reports. See id. § 1703(a)(1)(B). In October 1991, this court also granted partial summary judgment against the individual defendants as to Court III for violating the "anti-fraud provisions" of the Act, see 15 U.S.C. § 1703(a)(2)(B) and (C), and violating the Act's revocation requirements and their implementing regulations. See id. § 1703(b) and (c); 24 C.F.R. § 1715.2, and .3. The latter grant of

partial summary judgment was based entirely upon the absence of any material dispute as to the claims in Counts I and II. In other words, no additional disputes as to material fact were resolved. Because CCMV is in bankruptcy, this court did not enter judgment against it with respect to Count III.

HUD has proffered to the court a proposed judgment order. In light of the findings supporting this court's grants of summary judgment, the proposed order's permanent injunction against further sales in violation of the Act is appropriate. Without a permanent injunction, a reasonable likelihood exists that further violations would occur.

First, the violations alleged were not isolated or technical violations. Instead, they occurred in hundreds of transactions, and it is possible that absent the reporting violations the defendants would not have been able to sell the lots at Lake Monticello for inflated prices. See infra discussion at 7-8. In short, the violations constitute part of a pattern of conduct that suggests a strong propensity to repeat itself in the absence of a permanent injunction.

Second, the defendants appear to be absolutely unrepentant about their acts in violation of the statute. The court recognizes that a party's lack of remorse generally is not a proper factor for consideration in determining whether to impose a permanent injunction. However, the individual defendants twice in this case were certified in contempt by a magistrate judge. See Certification of Contempt (Jun. 29, 1990); Report & Recommendation (Feb. 7,

1991).[1] Although those rulings by the magistrate judge were mooted by the most recent grant of partial summary judgment, the court finds evidence in those decisions that the individual defendants do not feel bound by the orders of this court (or by the law). As such, consideration of the individual defendants' attitude towards these proceedings is a proper factor for consideration in imposing a permanent injunction. S.E.C. v. First City Financial Corp., Ltd., 890 F.2d 1215, 1229 (D.C. Cir. 1989). In light of these factors, a permanent injunction is appropriate and will issue in a separate order.

The court also does not question the appropriateness of a permanent injunction barring the defendants from enforcing any notes or other obligations issued by purchasers and held by defendants. This latter injunction is imposed for the reasons stated below in support of a remedy of restitution. Where restitution is a proper remedy, a court may properly exercise its equitable powers to enjoin the further unjust enrichment of the party who has committed the wrong. See Peterson, 940 F.2d at 114; S.E.C. v. Manor Nursing Centers, 458 F.2d 1082,

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[1] This Court on February 14, 1990 entered an injunction inter alia enjoining the individuals from transferring or disposing of their personal monies or assets except for the payment of reasonable living expenses, and required them to make financial reports to the magistrate judge on a monthly basis. The contempt findings arose from the individual defendants' failures to obey the asset freeze, and gave the Court cause for grave concern that the individual defendants had dissipated their assets by spending amounts far in excess of their personal incomes.

1103-04 (2d Cir. 1972);[2] Restatement of the Law, Restitution, Section 4 (1937). No evidence has yet been presented to establish that the defendants still hold the notes of purchasers, but if they do, setting aside those obligations will accomplish the purpose of terminating a continuing wrong.

A more difficult aspect of the proposed judgment order is its recommendation that the court order the individual defendants to make restitution of monies paid in connection with purchases of lots at Lake Monticello in an amount based upon the difference between the sale prices of the lots and the assessed value of the lots. See Manor Nursing Centers, 458 F.2d at 1104 (restitution is excess of what purchasers paid over value of what they received). The proposed order asks the court to establish a trust fund to receive such monies, and to appoint a trustee to disburse the monies to purchasers of lots in an amount proportional to the price of the individual purchaser's lot relative to the total price of the lots of all purchasers.[3] The order would also impose joint and several liability on the five individual defendants for an initial restitution payment of $100,000. Finally, upon this court's subsequent approval of a final judgment amount, all of the defendants would then become jointly and

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[2] The Act is patterned after the federal securities laws. Flint Ridge Dev. Co. v. Scenic Rivers Ass'n, 426 U.S. 776, 778 (1976). Therefore SEC cases have provided the parties and the court with useful precedent for the resolution of the questions at hand.

[3] This component of the proposed order is within the power of the Court to order. See Manor Nursing Centers, 458 F.2d at 1105 (upholding without explicit statutory authority appointment of trustee necessary to effectuate purposes of securities laws).

severally liable on a continuing basis to pay the final amount.

The individual defendants concede that restitution is a remedy available to HUD pursuant to 15 U.S.C. § 1714, and that disgorgement is a form of restitution. (Obj. to Prop. Order at 3). The defendants argue, however, that the remedy of disgorgement is only available where fraud is proven.[4] This position is incorrect for a number of reasons. First, the Act does not distinguish between the remedies available for violations of Section 1703(a)(1) (sales practices provisions), and § 1702(a)(2) (anti-fraud provisions). Second, this court has already granted partial summary judgment against the individual defendants for violating the anti-fraud provisions of the Act on the basis of their violations of registration and reporting requirements. See S.E.C. v. Benson, 657 F.Supp. 1122, 1130 (S.D. N.Y. 1987) (filing registration statement without disclosing a fact material to making the statement not misleading violates anti-fraud provision of Securities Act of 1933, 15 U.S.C. § 7q(a)). Third, "[i]t is for the federal courts to adjust their remedies so as to grant the necessary relief where federally secured rights are invaded." J.I. Case Co.

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[4] The Fourth Circuit has ruled in this case that an asset freeze must be supported by "a showing of fraud, mismanagement, or other reason to believe that...absent the freeze order, the assets would be depleted or otherwise become unavailable." Peterson, 940 F.2d at 114. It appears to this court that the Fourth Circuit directed its attention only to asset freezes, not to disgorgement, the court finds in the magistrate's contempt certifications ample reason to doubt that the assets of the individual defendants will be available to satisfy a judgment of restitution.

v. Borak, 377 U.S. 426, 433 (1964). This court has no doubt that it may properly order the defendants to disgorge the benefits they received as a result of their violations of the Act. It remains, however, for this court to consider in some detail certain problems raised by the imposition of an order of restitution and disgorgement.

I.

The first such problem relates to HUD's proposal that the individual defendants be required to make an initial restitution payment of $100,000. HUD has sought to demonstrate that $100,000 is an appropriate initial restitution by establishing that the ultimate liability of the defendants will be much greater than $100,000. HUD makes its proof by estimating the total number of lots sold in violation of the Act, their value, and their purchase prices. This evidence was presented in the form of a declaration by Roger G. Henderson, Director of the Interstate Land Sales Registration Division of HUD. According to the declaration, the defendants' own records indicate that at least 466 sales of lots were completed by the defendants. Two hundred and fifty eight of the 466 purchasers of those lots have responded to HUD questionnaires. The purchasers responses form the basis of the information provided in the Henderson declaration.

The declaration discloses that the average assessed valued of the 258 lots was $7,962. This information came from the Fluvanna County Commissioner of Revenue, whose tax assessments represent 100% of the

assessed values of the lots. Virginia by statutes requires that tax assessments of real estate be made at 100 percent fair market value. Va. Ann. Code Section 58.1-3201. The court therefore considers the county assessments to establish with a high degree of certainty the fair market value of the properties.[5]

Multiplying the average assessed value of $7,962 by the 466 lots yields a preliminary estimate that the total assessed value of the 466 lots was $3, 710,480. The actual assessed value of the lots purchased by the 258 questionnaire respondents was $2,054,300.

All 466 properties were sold between 1987 and 1989 in unimproved condition. The average price of the lots when sold by CCMV was $26,520. That is $18,558 more than the average assessed value of $7,962. Multiplying $26,520 by the 466 lots yields a preliminary estimate that the sum of the sale prices of the lots was $12,358,528. The difference between the $12,358,528 estimated total sale price for the 466 lots and the $3,710,420 estimated total assessed value is $8,648,048. More conservatively, the difference between the $6,842,275 total sale price for the 258 lots whose prices are known, and their $2,054,300 assessed value is $4,787,975.

HUD claims that because $8,648,048 is an approximation of the gross profit the

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[5] For purposes of the interim order, this degree of certainty is sufficient. If at a later proceeding the defendants are able to present to the court persuasive evidence that the assessments do not represent actual market value, the court will consider that evidence in arriving at a final judgment amount.

defendants received by virtue of their violations of the Acts provisions, it is not too much to require the individual defendants to make an initial restitution payment of $100,000 to the trust fund while the precise amount of restitution for which the defendants will be liable is finally determined by the court. The court agrees. In light of the certifications of contempt by the magistrate judge, and the likelihood that the individual defendants' ultimate liability will be substantially greater than $100,000, this court considers $100,000 to be a modest preliminary payment and a reasonable assurance that some restitution, (however inadequate) is forthcoming from the individual defendants.

II.

The court has taken quite seriously the individual defendant's argument that disgorement is a proper remedy only if proceeds of the illegal transactions can be shown to have passed through to them. Restitution is an equitable remedy consisting of a return to the innocent party of the dollar value of any benefit he conferred upon the other party. See Restatement of the Law, Restitution, Section 1, comment e (1937). The court therefore may only recover from the individual defendants restitution in an amount that can be shown to be equal to the benefit they received from CCMV as a result of the violations of the Act. See Manor Nursing Centers, 458 F.2d at 1104, S.E.C. v. Allen & Associates, Inc., 386 F.Supp. 866, 881 (S.D. Fla. 1974).

The proceeds of the land sales were not paid directly to the individual defendants' rather they passed through CCMV before reaching the individual defendants. CCMV now is in bankruptcy and will not therefore be subject to the interim judgment order accompanying this opinion. Ultimately, the evidence may show that the majority of chattel paper generated by the sales of lots at Lake Monticello was sold by CCMV to Northeastern Bank ("Northeastern").[6] The monies paid to CCMV by Northeastern in exchange for the obligations were probably used in part to satisfy CCMV's outstanding obligations for the lots it held in inventory, while the remainder was either retained or invested by CCMV, or paid as compensation to officers and employees of the corporation including the five individual defendants.

Beyond common sense, the history of this case suggests that a substantial amount of profits passed to the individual defendants as a result of their violations. Even after this court imposed its preliminary injunction freezing the individual defendants assets, the magistrate judge recommended that this court find them in contempt of court because their expenses went "beyond the pale of

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[6] Northeastern is a defendant in a separate class action before this Court alleging that it aided and abetted CCMV in its violations of the Act. Bailey v. Cost Control Marketing and Sales Management of Virginia, Inc., No. 89-0041-C (W.D. Va). That fact, however, and any potential recovery the class may have from Northeastern is irrelevant to this suit. The individual defendants are not co-defendants in this suit. The individual defendants are not co-defendants in that suit and there is no possibility of a double recovery against them.

reasonableness and constitute[d] a pattern of expenditure that far exceeds the income of each defendant." Report & Recommendation (Feb. 7, 1991). The purported gift by defendant James Marley to his son of $300,000 is but one egregious example. See Report & Recommendation (Oct. 16, 1990). The fact that defendants could conduct their financial affairs with so little restraint suggests that before the commencement of this action the individual defendants received sizable profits from the violations.

The Court of Appeals for the District of Columbia Circuit recently confronted a case in which it had to determine how a court should measure illegal profits for disgorgement purposes. See S.E.C. v. First City Financial Corp., Ltd., 890 F.2d 1215 (D.C. Cir. 1989). In that case, a corporate raider accumulated over five percent of a target company's shares on the open market without complying with the William's Act requirement that it report to the Securities and Exchange Commission within ten days of exceeding the five percent threshold. As a result, when the market finally discovered the takeover bid, the share prices rose sharply and the raider was able to sell the shares back to the target company for a profit measured by the district court at $2.7 million. The district court ordered disgorgement of the profit. The raider appealed the district court's measurement of the profit, arguing that its experts estimated the profits to be less than $100,000.

Discussing the burdens of proof in establishing profits to be disgorged from

violators of the securities laws, the court explained:

> Although the SEC bears the ultimate burden of persuasion that its disgorgement figure reasonably approximates the amount of unjust enrichment, we believe the government's showing of appellants' actual profits on the tainted transaction at least presumptively satisfied the burden. Appellants, to whom the burden of going forward shifted, were then obliged clearly to demonstrate that the disgorgement figure was not a reasonable approximation...
>
> ....
>
> ...Placing the burden on the defendants of rebutting the SEC's showing of actual profits, we recognize, may result, as it has in the insider trading context, in actual profits becoming the typical disgorgement measure. But the line between restitution and penalty is unfortunately blurred, and the risk of uncertainty should fall on the wrong doer whose illegal conduct created that uncertainty.

Id. at 1232. In future proceedings to determine the final amount to be disgorged, the court will be guided by these principles.

It may well be argued that First City is distinguishable from this case on the basis that the complicating factor in the profit determination there was quite different from the pass-through problem here. In First City the district court had calculated the profits that resulted from the Williams Act violation by simply calculating all of the profits the

raider realized (in its eventual sale back to the target company) on the stocks it purchased after the date it should have provided statutory notice to the SEC. The appellant raider objected to this calculation because it omitted consideration of four factors that drove the share prices up but which did not result directly from the failure to notify the SEC of the takeover bid. If these factors had been considered by the court, its determination of the profit that resulted from the violation would have been considerably less.

In the case at bar, the complicating factor is not a volatile market influenced by innumerable variables, but the ability of a corporate defendant to disperse its profits by compensating its officers and employees. In spite of this factual distinction, First City remains very persuasive authority. The D.C. Circuit resolved the First City case using generalized reasoning applicable in this case. It upheld the district court, explaining that "[r]ules for calculating disgorgement must recognize that separating legal from illegal profits exactly may at times be a near-impossible task. Accordingly, disgorgement need only be a reasonable approximation of profits causally connected to the violation." Id. at 1231 (citation omitted). First City thus provides this court with a standard governing the degree of precision (or lack thereof) with which this court must proceed in determining the preliminary and final dollar amounts to be disgorged.

Aside from suggesting that the permissible margin of error is substantial, First City also presents a solution to the

dilemma of determining how much "profit" ultimately passed to the individual defendants. At the appropriate time, the court will calculate the gross compensation each individual defendant received from CCMV over a period yet to be determined, including but not limited to salary, commission, bonuses, loans and stock dividends. The result will be a reasonable approximation of the profits causally connected to the violations[7] and received by each individual defendant. The court rejects n these grounds HUD's proposal that the individual defendants incur continuing, joint and several liability for providing restitution of the entire profits of CCMV arising from the violations.

This court concludes that $100,000 is a reasonable preliminary approximation of the amount ultimately to be disgorged. It is reasonable from the perspective of the individual defendants because of the overwhelming likelihood that it understates their ultimate liability. It is also reasonable to them because they can recover restitution paid into the fund upon an adequate evidentiary showing. The $100,000

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[7] The facts before the Court create a strong presumption that a substantial portion of CCMV's net earnings accrued as a result of its failure to comply with the Act's requirements. A conservative estimate of profits causally related to the statutory violations committed at Lake Monticello suggests that they may amount to 4.7 million dollars. See Supra discussion at ___. the point to be made here, however, is that unless CCMV establishes that it received revenues not causally connected to the violations (for example by showing that only half of CCMV's gross revenues were related to its operations at Lake Monticello), all of its profits will be considered connected to the violations. Therefore all compensation paid to officers and employees will also be considered causally related to the violations.

initial restitution payment is not a final judgment. The Fourth Circuit held in an interim appeal in this case that the asset freeze this court imposed was proper regardless of traceability of profits because it was a preliminary remedy. See Peterson, 940 F.2d at 113-14. If the court finds that any individual defendant contributed more to the trust fund than the amount by which he was unjustly enriched, the fund will restore the amount by which he was unjustly enriched, the fund will restore the amount by which he was unjustly enriched, the fund will restore the excess to him. Finally, the order of initial restitution is reasonable in light of the strong evidence presented by the magistrate judge who administered the asset freeze that the individual defendants cannot be trusted to conserve their assets.

An appropriate Order shall this day issue.

Entered: /s/ James H. Michael, Jr.
Judge
April 22, 1992
Date

IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF VIRGINIA
CHARLOTTESVILLE DIVISION

JACK KEMP, SECRETARY OF THE
DEPARTMENT OF HOUSING AND
URBAN DEVELOPMENT,

Plaintiff

v.

COST CONTROL MARKETING AND
SALES MANAGEMENT OF VIRGINIA,
INC., et al.,
Defendants

Civil Action No. 89-0042-C

Entered April 22, 1992

INTERIM JUDGMENT ORDER

JUDGE JAMES H. MICHAEL, JR.

Upon consideration of the parties' arguments relating to the nature of an appropriate equitable remedy against the individual defendants, William Peterson, Arthur Kujawski, James Marley, Richard Costenbader, and Thorton Bryon, it is this day

ADJUDGED AND ORDERED

that:

1) The individual defendants shall be, and they hereby are, permanently enjoined

from enforcing any obligation to pay in any contract, deed of trust, or note held by these defendants and entered into between any purchaser and any defendant in connection with purchases of lots at Lake Monticello.

2) The individual defendants shall be, and they hereby are, ordered to make restitution of profits received by each of them individually in connection with sales of lots at the Lake Monticello subdivision in violation of the Interstate Land Sales Full Disclosure Act.

3) The amount of said profits received by the defendants individually shall be initially determined by the United States Magistrate Judge B. Waugh Crigler pursuant to 28 U.S.C.§636(b)(1)(B) in accordance with the accompanying Memorandum Opinion, and may be established by the Secretary using evidence of compensation of the individual defendants by CCMV or other transfers of money or property to the individual defendants from CCMV or other parties or non-parties in connection with the defendants' action as agents of CCMV. The Secretary may present evidence of, but not limited to, compensation paid by CCMV to the individual defendants including salaries, commissions, bonuses, dividends, loans, or any other incentive or reward received by them in any form from CCMV or any other entity in relation to CCMV's lot sales at Lake Monticello. Such compensation or transfers as may be considered shall be limited, except for good cause shown, to those made subsequent to the sale by CCMV of its first lot at Lake Monticello in violation of the Act.

4) Each purchaser of a lot at Lake Monticello will be paid a portion of the

total amount in the trust fund described below, based on the price of the purchaser's lot relative to the total price of the lots of all purchasers.

5) A Trustee shall be appointed by the Court to oversee the restitution process; the individual defendants shall be jointly and severally liable to pay all costs associated with administering the trust, and must pay such costs within thirty days of receipt of any bill from the Trustee for such costs. To the extent that any other co-defendant becomes liable for restitution in the future, such defendant shall be liable to the individual defendants for a reasonable contribution towards the initial costs of establishing the trust.

6) The Trustee may, within his or her discretion, make annual disbursements from monies received from any defendants ordered to make restitution to purchasers of lots from CCMV at Lake Monticello.

7) No later than thirty days following the entry of this Order, the individual defendants shall be jointly and severally liable for a deposit of $100,000 with Trustee as an initial payment of the full amount due.

8) Upon approval by this Court of a final amount of restitution to be made by each individual defendant, those defendants shall thereafter be individually liable to pay such amount to the Trustee within 90 days of the entry of the order, with a continuing obligation to pay thereafter, and interest shall accrue on any unpaid amount at the treasury rate until the judgment is paid in full.

9) If full payment is not submitted to the Trustee within 90 days as required, defendants Peterson, Marley, Kujawski, Costenbader, and Byram, are hereby ordered to make restitution of the monies found by the Court to be owing by them individually, according to the following formula: each year for the seven years from calendar year 1992 through 1998, each defendant shall remit by April 30 of the following year 30% of that defendant's adjusted gross income as reported on that defendant's federal income tax return. If, at the end of seven years, the defendants have still not made full payment of their individual restitution judgments, the defendants shall remain jointly and severally liable for the remainder, and interest shall continue to accrue on the unpaid amount at the annual treasury rate until paid.

10) Each of the defendants shall file an affidavit with the Secretary and with the Trustee, beginning 30 days after the entry of this Order, and continuing annually until full restitution has been made as described above, containing the following information: a listing of all assets and liabilities as of the date the affidavit is filed; current business and home addresses and telephone numbers; monthly and/or annual salary; a list of all income other than salary; and a listing of all bank accounts, including the name of the bank, branch, the account number, and current balance.

11) Paragraph (4) of this Court's Order entered on October 19, 1992 shall be, and it hereby is, vacated, and the asset freeze and sequestration imposed by Order

entered February 14, 1991 is hereby reinstated under the same terms.

The Clerk of the Court is hereby directed t send a certified copy of this Order to all counsel of record.

ENTERED: /s/James H. Michael, Jr.
Judge

April 22, 1992
Date

IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF VIRGINIA
CHARLOTTESVILLE DIVISION

JACK KEMP, Secretary
of Housing and Urban
Development,

Plaintiff

v.

COST CONTROL MARKETING
AND SALES MANAGEMENT
OF VIRGINIA, INC., a
Virginia Corporation,

Defendants.

Civil Action No. 89-0042-C

Entered November 30, 1992

ORDER

By: B. WAUGH CRIGLER
U.S MAGISTRATE JUDGE

Pursuant to a status conference held on November 18, 1992, is

O R D E R E D

as follows:

1. Plaintiff shall have until December 18, 1992 within which to petition the Bankruptcy Court for the Middle District of

Pennsylvania to lift the automatic stay as to defendants Peterson, Costenbader and Marley so that this court may proceed to an adjudication of the actual amount of their liability under the judgment heretofore entered in this action.

2. On or before December 18, 1992, all defendants other than Peterson, Costenbader and Marley shall show cause to this court why he or it has failed to comply with the injunction entered by the presiding District Judge Requiring the deposit of $100,000.00 in an account overseen by the court.

The Clerk of the Court is hereby directed to send a certified copy of this Order to all counsel of record.

ENTERED: /s/ B. Waugh Crigler
Magistrate Judge
November 30, 1992
Date

IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF VIRGINIA
CHARLOTTESVILLE DIVISION

HENRY G. CISNEROS, SECRETARY OF THE DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT,

Plaintiff

v.

COST CONTROL MARKETING AND SALES MANAGEMENT OF VIRGINIA, INC., ET AL.,

Defendants

Civil Action No. 89-0042-C

REPORT AND RECOMMENDATION

By: B. WAUGH CRIGLER
U.S. MAGISTRATE JUDGE

Entered July 27, 1994

After some five (5) years of litigation, numerous hearings before this court and the presiding District Judge, and at least one appeal to the Fourth Circuit Court of Appeals, this action is before the court on the January 7, 1994 motions of the Secretary for the entry of final judgment, the award of sanctions under Fed. R. Civ. P. 37(d) and a finding of contempt as the result of the alleged failure of the defendants to comply with the presiding District Court's interim judgment entered on April 22, 1990. The Secretary also filed a notice of dismissal of

Thornton Byron on January 7, 1994 to which no other party has filed an objection. Defendants, however, to oppose the entry to final judgment on various grounds, the most prominent of which are that plaintiff has failed to produce sufficient evidence to prove damages with any degree of reasonableness, and that the interim judgment of the court was discharged against defendants Peterson, Marley and Costenbader by the Bankruptcy Court for the Middle District of Pennsylvania.[1] These objections will not long detain this court, nor should they cause the presiding District Judge to tarry long; they are without merit.

DISMISSAL OF THORNTON BYRON

There having been no objection to the Secretary's notice of dismissal of Thornton Byron, it is

RECOMMENDED

that the court voluntarily dismiss plaintiff's action against Thornton Byron under Fed. R. Civ. P. 41(a)(1)(i).

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[1] Defendants also believe that any entry of a final order would be contrary to decisional authority relating to restitution and disgorgement and will violate the decision by the Fourth Circuit Court of Appeals in Kemp v. Cost Control Mktg. & Sales Mgt., Record No 90-2049. They further assert that restitution is not available as a fine or penalty, and that the entry of final judgment will violate defendants' due process rights. These contentions have no support in the law and should be rejected out-of-hand.

EFFECT OF BANKRUPTCY

This court has concurrent jurisdiction with the bankruptcy court to determine whether the automatic stay applies and whether any defendant's debt is dischargeable or has been discharged in bankruptcy. *See, e.g., Picco v. Global Marine Drilling Co.*, 900 F.2d 846 (5th Cir. 1990); *Brock v. Morysville Body Works, Inc.*, 829 F.2d 383 (3rd Cir. 1987); *In re Baldwin-United Corp. Litig.*, 765 F.2d 343 (2nd Cir. 1985). It is recognized that where concurrent jurisdiction exists, the court which first had possession of the subject matter must decide. *United States Fire Ins. Co. v. Goodyear Tire and Rubber Co.*, 920 F.2d 487 (8th Cir. 1990); *EEOC* v. University of *Pa.*, 850 F.2d 969 (3d Cir. 1988); *see also, Kline v. Burke Constr. Co.*, 260 U.S. 226 (1922). This court had first possession of the subject matter of this case, and it should determine whether any proceedings should be stayed and whether the debt was discharged to any extent.

Excepted from the automatic stay of bankruptcy proceedings are the "commencement or continuation of an action or proceeding by a governmental unit to enforce such governmental unit's policy or regulatory powers." 11 U.S.C. §362(a)(1), 362(b)(4). To put it differently, a proceeding by the government to enforce its police or regulatory powers is not stayed automatically by the filing of bankruptcy, especially where there has been, is, or will be fraud, and even where the action is an attempt to prevent or stop violations or the law, or to fix damages for violations of the law. In re. Poule, 91 B.R. 83 (9th Cir. 1988). S.

Rep. No. 989, 95th Cong., 2nd Sess. 52, reprinted in 9178 U.S.C.C.A.N. 5787, 5838. Here, there were clear violations of the Interstate Land Sales Full Disclosure Act (Act), 15 U.S.C. §1701, et. seq., which is aimed at the very activity that has been the subject of this action deterring fraudulent conduct in interstate land sales.

Furthermore, the automatic stay does not apply to "enforcement of a judgment, other than a money judgment, obtained in an action or proceeding by a governmental unit to enforce such governmental unit's police or regulatory power. 11 U.S.C. §362(b)(5). Although this language suggests that enforcement of a money judgment would remain stayed, it does not apply to this case. Section 362(b)(5) only applies to enforcement...of a judgment obtained before the commencement of the [bankruptcy]case...." Id. §362(a)(2) (emphasis added). The defendants' bankruptcy cases clearly were commenced before the entry of judgment.[2]

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[2] If §362(b)(5) did apply to this case, then the monetary part of the judgment could not be enforced at this time against Peterson, Marley, and Costenbader. Although the restitution sought by the plaintiff is penal in nature, the term "money judgment" as used in §362(b)(5) seems to include payment of money, for whatever reason, to a governmental unit acting within its police or regulatory powers. Compare Penn Terra Ltd. v. department of Envtl. Resources, 733 F.2d 267 (3d Cir. 1984) (holding that an injunction to correct environmental violations which requires the expenditure of funds is not a money judgment within §362(b)(5) with Ohio v. Kovacs, 469 U.S. 274, 283 n.11 (1985) (distinguishing Penn Terra from a case in which state appointed a receiver to collect money from bankrupt to be used to clean up hazardous waste disposal site because "enforcement of such a judgment by seeking money from the bankrupt" is different from an injunction requiring compliance with state laws); se also EEOC v.

Enforcement of the judgment, however, is not a concern for this court at this time.

It is also clear that a debt which is a fine, penalty, or forfeiture payable to a governmental unit, and is not compensable for actual pecuniary loss...is not discharged in bankruptcy. 11 U.S.C. 524(a)(2). Furthermore, an order of restitution does not constitute a debt dischargeable in bankruptcy. *Pennsylvania Pub. Welfare Dept. v. Davenport*, 495 U.S. 552 (1990); *Kelly v. Robinson*, 479 U.S. 36 (1986).

To fall within the exception for fines, penalties and forfeitures, the debt: 1) must be to and for the benefit of the governmental unit, and 2) must be penal, rather then pecuniary, in nature. Kelly, 479 U.S. at 51-52. The presiding District Judge already has recognized that the Act at issue is patterned after federal securities laws. *Kemp v. Cost Control Mktg. and Sales Mgt.*, 790 F. Supp. 1275, 1277 n.2. Therefore, enforcement of it by restitution surely would be for the benefit of HUD, the governmental unit in this action. In addition, pursuit of the judgment in this case has been driven by a desire to punish defendants for their clear violations

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McLean Trucking Co., 834 F.2d 398 (4th Cir. 1987) (holding that back pay awards are money judgments and thus enforcement of the award is stayed by bankruptcy). But see United States v. Troxler hosiery Co., Inc., 41 B.R. 457, 459 (Bankr. W.D.N.C. 1984) (holding that criminal fines are not stayed by §362(b)(5) because based on the criminal nature of the fines they are not actions by a governmental unit to enforce its police or regulatory powers), aff'd, 796 F.2d 723 (4th Cir. 1986), cert. denied, 480 U.S. (1987).

of the law and to serve as a deterrent of the Act, not by a desire for victim compensation.[3]

To summarize, this court is of the view that plaintiff's judgment in this court is not dischargeable in bankruptcy, and the automatic stay does not apply. Therefore, it is

RECOMMENDED

that defendants' objections on bankruptcy grounds to this court's authority to enter final judgment be denied.

ENTRY OF FINAL JUDGMENT

The Interim Order entered some twenty-six (26) months ago set forth the components that should comprise the final order, and in it Judge Michael held that plaintiff had satisfied its initial burden of showing a reasonable approximation of the defendants' unjust enrichment. *Kemp*, 790 F. Supp. at 1278-79. The burden then shifted to defendants to offer evidence showing that not all CCMV's profits connected with violations of the Act passed through to them. Without that evidence, "all compensation paid to the officers and employees will...be considered causally related to the violations. "*Id.* at 1281 n.7.

It is not an overstatement to say that defendants have done nothing to discharge their burden. They have not answered interrogatories, and they have not submitted

[3] One might observe that if compensation of the victims had been a true goal of the plaintiff, it did little to achieve that goal over the five (5) years that this case, or some version of it, has been pending either before this court or the Fourth Circuit Court of Appeals.

evidence of their own. More telling is the active efforts on the part of some of them to frustrate enforcement of any final judgment which the plaintiff is entitled to receive. The clock has been ticking, and time has run out.

There is an absence of anything of substance that would suggest that the fair approximation made by the presiding District Judge should not stand as the figure to award in final judgment.[4] The figure may be more than the actual amount of profits received by the defendants, but they have had an ample opportunity to demonstrate a more reasonable sum and have not done so. It is this court's view that the reasonable estimate of the government should prevail. *See SEC v. First City Finan. Corp., Ltd.*, 890 F.2d 1215 (D.C. Cir. 1989).

Therefore, it is

RECOMMENDED

that final judgment enter in the amount of Eight Million Six Hundred Forty-eight Thousand Forty Eight and 00/100 Dollars ($8,648,048.00) in favor of the plaintiff and against the defendants, and each of them jointly and severally.

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[4] The only thing ever offered by defendants during the course of this case has been argument of counsel, which is just that, argument of evidence. There never has been a stitch of substance to any of the positions taken by counsel on the merits of the case, and nothing has changed when it has come to assessing the amount to be entered as final judgment in the case.

SANCTIONS AND CONTEMPT

It is the considered opinion of this court that nothing will be achieved by the entry of further sanctions against the defendants than will be achieved by a final disposition of the case. The court could have premised its recommendation for entry of final judgment as a sanction against the defendants for failure to conduct discovery, but the merits of plaintiff's claim on the extant record just does not seem to justify further inquiry.

This court also questions the utility of contempt at this juncture in the case. What the parties to this case, and the court for that matter, need more than anything after five years of litigation is closure. The court should now let this "Sleeping dog lie". It is, therefore,

RECOMMENDED

that an order enter denying plaintiff's motion for sanctions and order of contempt.

The clerk hereby is directed immediately to transmit the record in this case to the Hon. James H. Michael, Jr., United States District Judge. Both sides are reminded that Rule 72(b) entitles them to note any objection they may have to this Report and Recommendation within ten (10) days hereof. Any adjudication of fact or conclusion of law rendered herein by the undersigned not specifically objected to within the period prescribed by law may become preclusive upon the parties. Failure to file specific objections pursuant to 28 U.S.C. §636(b)(1)(C) as to factual recitations or

findings as well as to the conclusions reached by this court may be construed by any reviewing court as a waiver of such objection.

The clerk further is directed to send a certified copy of this Report and Recommendation to all counsel of record.

ENTERED: /s/ B. Waugh Crigler
Magistrate Judge

July 7, 1994
Date

IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF VIRGINIA
CHARLOTTESVILLE DIVISION

HENRY G. CISNEROS, SECRETARY
OF THE DEPARTMENT OF HOUSING
AND URBAN DEVELOPMENT

Plaintiff

v.

COST CONTROL MARKETING AND SALES MANAGEMENT
OF VIRGINIA, INC., et al.,

Defendants

Civil Action No. 89-0042-C

MEMORANDUM OPINION

Entered September 15, 1994

This Court referred this case to the Honorable B. Waugh Crigler, United States magistrate Judge, for proposed findings of fact and a recommended disposition. The Magistrate Judge filed his Report on July 27, 1994. On August 8, 1994 and August 12, 1994 the defendants filed Objections to the Report and Recommendation. Said objections having been lodged with this court in a timely and appropriate manner, this court is required to undertake a de novo determination. Orpiano v. Johnson, 687 F.2d 44, 48 (4th Cir. 1982).

The defendants' liability in this case has been established for some time, but

remaining before the court is a decision concerning the character and amount of the final judgment. Magistrate Judge Crigler's July 27, 1994 Report and Recommendation found that this court has the authority to enter final judgment, notwithstanding the current bankruptcy proceedings involving the individual defendants Peterson, Marley, and Costenbader. Furthermore, Magistrate Judge Crigler recommended entering final judgment against the above-named defendants and defendant Kujawski in the $8, 648,048, although he declined to do so on the basis of the plaintiff's motions for sanctions and contempt.[1] This court adopts both the reasoning and the decision set forth in Magistrate Judge Crigler's July 27, 1994 Report and Recommendation.

I.

The plaintiff instituted this action against the defendants for violations of the Interstate Land Sales Full Disclosure Act, 15 U.S.C. §§ 1701-1720, committed during their sales of lots in Lake Monticello. The court entered summary against the defendants for violating the Act's anti-fraud provisions and then turned to the task of structuring a final judgment. See Kemp v. Cost Control

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[1] This court agrees with Magistrate judge Crigler that holding the defendants in contempt and imposing sanctions, although perhaps justified, would be counterproductive. Given the present entry of final judgment, the only possible sanction would be their restitution obligations. In addition, Magistrate Judge Crigler recommended that the court voluntarily dismiss defendant Thornton Byron from this case. In its accompanying Order, the court also will adopt these recommendations.

Mktg. & Sales Mgt., 790 F. Supp 1275 (W.D. Va. 1992) (entering interim judgment). Subsequent to the entry of an Interim Judgment Order on April 22, 1992, defendants Peterson, Marley, and Costenbader filed Chapter 7 bankruptcy petitions in the Western District of Pennsylvania. Although such bankruptcy petitions were discharged in January of 1993, the three defendants reopened their bankruptcy cases on may 20, 1994 for the purpose of enjoining the plaintiff from any further proceeding against them. Based upon their bankruptcy cases, these defendants have asserted that this court has no authority to enter final judgment against them. They are wrong.

In general, a bankruptcy petition stays the continuation of a pre-petition judicial action, 11 U.S.C. § 362(a)(1) and the enforcement of a pre-petition judgment against the debtor, 11 U.S.C. §362(a)(2); however, several exceptions to the stay exist. In addition, upon discharge of a bankruptcy petition, 11 U.S.C. §524(a)(2) discharges all debts of the bankrupt, again subject to several exceptions. The issue is whether certain such exceptions apply to this case.

This court and the bankruptcy court share concurrent jurisdiction to determine whether the automatic stay applies to this proceeding and whether the defendants' debts to the plaintiff are dischargeable. See Picco v. Global Marine Drilling Co., 900 F.2d 846, 850 (5th Cir. 1990); Brock v. Morysville Body Works, Inc. 829 F.2d 383, 387 (3d Cir. 1987); NLRB v. Edward Cooper Painting, Inc., 804 F.2d 934, 936 (6th Cir. 1986); Hunt v. Bankers Trust Co., 799 F.2d 1060, 1069 (5th

Cir. 1986); In re Baldwin - United Corp. Litig., 765 F.2d 343, 347 (2d Cir. 1985). Furthermore, defendants' objections to the contrary notwithstanding, long-standing principles of comity suggest that it is appropriate for this court, rather than the bankruptcy court, to decide the issue because the proceeding was first filed in this court. See Smith v. McIver, 22 U.S. (9 Wheat) 532, 535 1824) (*[I]n all cases of concurrent jurisdiction, the court which first has possession of the subject must decide it."); see also United States Fire Ins. Co. v. Goodyear Tire & Rubber Co., 920 F.2d 487, 488 (8th Cir. 1990); EEOC v. University of Pa., 850 F.2d 969, 972 (3d Cir. 1988) (citing Kline v. Burke Constr. Co., 260 U.S. 226, 229 (1922)). This court has been handling this case for approximately five years and, therefore, presumably is more familiar than the bankruptcy court with the nature of the action. Consequently, this court is the appropriate forum in which to decide whether the automatic stay applies to this case and whether the defendants' debt to the plaintiff is dischargeable in bankruptcy.

The automatic stay imposed by §362(a)(1) does not apply to "the commencement or continuation of an action or proceeding by a governmental unit to enforce such governmental unit's police or regulatory powers." 11 U.S.C. § 362(b)(4). Included in the government's "police or regulatory powers" are situations "where a governmental unit is suing a debtor to prevent or stop violation of fraud...laws, or attempting to fix damages for violations of such a law>>>>" S. Rep. No. 989, 95th cong., 2d Sess. 52, reprinted in 1978 U.S.S.C.A.N. 5787, 5838.

In such a case, the action is not stayed. Id. In this case, the defendants violated the Interstate Land Sales Full Disclosure Act (the Act), 15 U.S.C. §§ 1701-1720, which is aimed at halting, deterring, and punishing fraudulent conduct in interstate land sales.[2] Pursuant to its power granted by 15 U.S.C. §1714, the plaintiff filed this suit for the purpose of punishing the defendants for fraudulent practices and deterring any similar conduct in the future. Based upon the scope of the Act and particular character of this case, suing the defendants for violating the Act is within the plaintiff's "police or regulatory powers." As a result, this action is excepted from the automatic stay pursuant to 11 U.S.C. §362(b)(4).[3]

Furthermore, although a bankrupt's debts generally are discharged when a bankruptcy case is discharged, 11 U.S.C. §524(a)(2), an exception is made for a debt which is "a fine, penalty, or forfeiture payable to and for the benefit of a governmental unit, and

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[2] In particular, the defendants (1) failed to file with the plaintiff a Statement of Record, in violation of 15 U.S.C. §1703(a)(1)(A); (2) sold lots without providing purchasers with Property Reports, id. §1707; and (3) engaged in fraudulent sales practices, in violation of both the Act's "anti-fraud provisions" id. §1703(a)(2)(B), (C), and the Act's revocation requirements, id. §1703(b), (c); 24 C.F.R. §1715.2, .3.

[3] Enforcement of this judgment currently is not an issue before this court. The three defendants who reopened their bankruptcy cases did so for the limited purpose of enjoining this action. As a result, their bankruptcy cases likely will close very soon, thus mooting any issue as to enforcement. The court notes, however, that 11 U.S.C. §362(b)(5), which excludes the enforcement of money judgments from the exception to the automatic stay, is expressly tied to §362(a)(2), which only stays enforcement of judgments obtained before the filing of a bankruptcy petition.

is not compensation for actual pecuniary loss.... "Id. §523(a)(7). The character of the plaintiff's monetary recovery in this case, restitution in the form of disgorged profits, clearly is covered by §523(a)(7). The supreme court plainly has held that a restitution obligation is not dischargeable in bankruptcy because it falls within §523(a)(7). Kelly v. Robinson, 479 U.S. 36, 52 (1986). Although Kelly dealt with criminal restitution, the Court later made clear that §523(a)(7) applies both to criminal and civil restitution. See Pennsylvania Public Welfare Dept. v. Davenport, 495 U.S. 552, 562 (1990) (stating that §523(a)(7) codified an exception for both criminal and civil fines).[4]

In finding that § 523(a)(7) applies to restitution obligations, the Supreme court stated that in order to be excepted from discharge, debts must satisfy two requirements: (1) they must be to and for the benefit of a governmental unit; and (2) they must be penal, rather than pecuniary, in nature. Kelly, 479 U.S. at 51-52. The judgment in this case satisfies both parts of the test. The first prong is satisfied

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[4] In their objection of August 8, 1994 the defendants suggest that Davenport actually supports their position that their obligation to the plaintiff was discharged. In Davenport, the Supreme Court held that restitution obligations constitute "debts" as defined in the Bankruptcy Code and are thus dischargeable in Chapter 13 bankruptcy cases. The Court expressly stated that the debts were dischargeable in Chapter 13 cases because §523(a)(7) does not apply to that chapter. See Davenport, 495 U.S. at 563. Chapter 7, pursuant to which the defendants filed their bankruptcy petitions, contains the §523(a)(7) exception to discharge, and restitution obligations thus are not dischargeable by Chapter 7 cases. Id.

because restitution ensures compliance with the Act and safeguards the public interest in such compliance. "To permit the retention of...illicit profits...would impair the full impact of the deterrent force that is essential if adequate enforcement of (the Act) is to be achieved." SEC v. Petrofunds, Inc., 420 F. Supp. 958, 960 (S.D.N.Y. 1976).[5] Likewise, the second prong is satisfied because the restitution sought in this case is penal in nature and is not driven by the victims' desire for compensation. The money will be paid to the plaintiff rather than the injured victims, and the judgment will punish the defendants for violations of the Act and deter future violations by the defendants and others. Whether any of the money reaches the victims is immaterial to the §523(a)(7) analysis. See Kelly, 479 U.S. at 52. Because the automatic stay does not apply to this case and because the defendants' restitution obligation is not dischargeable, this court has authority to enter final judgment.

II.

The general elements that comprise the final judgment are contained in the Interim Judgment Order entered on April 22, 1992. See Kemp v. Cost Control Mktg. & Sales Mgt., 790 F. Supp. 1275 (W.D. Va. 1992). Since that time, the defendants have had twenty-seven months in which to present evidence to

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[5] Although Petrofunds concerned an SEC enforcement action, this court already has recognized that the Act is patterned after federal securities laws. See Kemp, 790 F. Supp. at 1277 n.2 (citing Flint Ridge Dev. Co. v. Scenic Rivers Ass'n, 426 U.S. 776, 778 (1976)).

challenge the court's preliminary findings contained in Kemp. They have not done so.

This court previously ruled that in determining the amount of profits to be disgorged, it will be guided by SEC v. First City Financial Corp., Ltd., 890 F.2d 1215 (D.C. Cir. 1989). Accordingly, although the plaintiff bears the burden of proving a figure that reasonably approximates the illegal profits received by the defendants, upon satisfaction of that initial burden the defendants are obligated to demonstrate that such amount is not a reasonable approximation of illegal profits received. Kemp, 790 F. Supp. at 1280 (citing First City, 890 F.2d at 1232). This court already has found that $8,648,048 is a reasonable approximation of the illegal profits received by Cost Control Marketing and Sales Management of Virginia (CCMV), id. at 1278-79, and that in the absence of additional evidence "all compensation paid to officers and employees will...be considered causally related to the violations [of the Act].' Id. at 1281 n.7.

The plaintiff also bore the burden of proving a reasonable approximation of the amount of CCMV's profits passed through to the defendants. See id. at 1279-80. The court found, however, that the financial habits of the defendants show that "a substantial amount of profits passed to the individual defendants as a result of their violations." Id. This evidence and the principle that in demonstrating the amount of profits for the purpose of disgorgement "the permissible margin of error is substantial," id. at 1281, satisfied the court that, in the absence of any contrary evidence, the figure of $8,648,048 is sufficient to discharge the

plaintiff's initial burden of proving a reasonable approximation of the defendants' illegal profits.[6] The court delayed the entry of final judgment in order to allow the defendants an opportunity to offer evidence showing that part of that amount was not passed through from CCMV to them.

The defendants have presented absolutely nothing in response to the plaintiff's evidence. Twenty-seven months have passed since the court issued its Interim Judgment Order, and the defendants virtually have ignored it. Not only did they fail to comply with the terms of the Interim Judgment Order, but all except one of them failed even to respond to the court's Order to Show Cause for not complying. Further, the defendants have failed to respond to the plaintiff's two year-old interrogatories and requests for production of documents designed to obtain a more exacting measure of the illegal profits received by the defendants. The defendants contend that they believed that their bankruptcy cases stayed this case. Their bankruptcy cases were closed from January of 1993 until May of 1994, however, and the defendants still disregarded their obligations. Moreover, even if the defendants genuinely believed that these proceedings were stayed during the course of their bankruptcy cases, the court's Order to Show Cause and continued movement toward the

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[6] The court also notes that CCMV, a company primarily operated by the individual defendants, has declared bankruptcy despite receiving over $8 million in illegal profits. It is more than reasonable to conclude that a vast portion of those illegal profits were passed through to individuals who controlled the company and enjoyed excessive spending patterns while their primary source of income went bankrupt.

entry of final judgment against the individual defendants[7] made clear that it did not necessarily agree. Lastly, the court notes that it does not regard the defendants' failure to respond to the plaintiff's discovery requests as a reason to enter final judgment, but merely as another example of the countless opportunities that the defendants have had to present evidence concerning the amount of illegal profits that they received.

The defendants also contend that this case is affected by a separate class action regarding the same fraudulent land sales at issue here. First, the allege that the class action imposed a stay which prevents this court from entering final judgment. Any stay imposed in that case or any other, however, did not apply to these individual defendants. Secondly, the defendants contend that a settlement effectuated in the class action obviates the need for restitution in this case.[8] The defendants misunderstand the nature of this action. The restitution in this case is a penalty, not compensation to injured victims. That individual victims may have been partly compensated for their losses is irrelevant. Although the plaintiff has expressed its intention to use the restitution paid to it to reimburse the victims for their losses, if it finds that a particular victim has been reimbursed, it may choose to apply any excess to things such as

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[7] Magistrate Judge Crigler held a status conference concerning the entry of final judgment, and the court has received several pleading from the parties directed to that issue.

[8] These individual defendants will contribute nothing to that settlement.

interest, travel to and from the lot, or other related expenses incurred by the victims. Cf. 15 U.S.C. § 1709 (listing amounts recoverable in a civil action by an injured person).

No reason exists to delay any longer the entry of final judgment. This case has endured for approximately five years, and the defendants' liability has been established for roughly half of that time. Because the defendants' bankruptcy cases do not prevent the entry of final judgment, and because the defendants have presented no evidence to suggest that the plaintiff's figure is not a reasonable approximation of their illegal profits, final judgment will be entered against the individual defendants in the amount of $8,648,048.

An appropriate Order shall this day issue.

ENTERED: /s/ James H. Michael, Jr.
Judge

September 15, 1994
Date

IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF VIRGINIA
CHARLOTTESVILLE DIVISION

HENRY G. CISNEROS, SECRETARY
OF THE DEPARTMENT OF HOUSING
AND URBAN DEVELOPMENT

Plaintiff

v.

COST CONTROL MARKETING AND
SALES MANAGEMENT OF VIRGINIA
INC., et al.,

Defendants

CIVIL ACTION NO. 89-0042-C

ORDER

JUDGE JAMES J. MICHAEL., JR

Entered September 15, 1994

For the reasons stated in the accompanying Memorandum Opinion, it is this day

ADJUDGED AND ORDERED

1. The objections to the Report and Recommendation of the United States Magistrate Judge are overruled, and said Report, filed July 27, 1994, shall be, and it hereby is, adopted in its entirety.

2. For the reasons stated in the Magistrate Judge's Report the plaintiff's motion to voluntarily dismiss defendants

Thornton Byron, shall be, and it hereby is, granted.

3. For the reasons stated in the Magistrate Judge's Report, the defendants' objections on bankruptcy grounds to this court's authority to enter final judgment shall be, and they hereby are, denied.

4. For the reasons stated in the Magistrate Judge's Report, the plaintiff's motions for sanctions and contempt shall be, and they hereby are, denied.

5. For the reasons stated in the Magistrate Judge's Report, defendants Peterson, Kujawski, Marley, and Costenbader, jointly and severally, shall be, and they hereby are, ordered to make restitution in the amount of eight million six hundred forty-eight thousand forty-eight and 00/100 dollars ($8,648,048.00), payable to the Department of Housing and Urban Development or its successor agency ("the Department"), in a manner consistent with the terms of this Order.

6. Defendants Peterson, Kujawski, Marley, and Costenbader, as well as all individuals and entities acting in concert or participation with any of them, shall be, and they hereby are, permanently enjoined from violating the Interstate Land Sales Full Disclosure Act, 15 U.S.C. §§1701-1720, and its implementing rules and regulations.

7. Defendants Peterson, Kujawski, Marley, and Costenbader shall be, and they hereby are, permanently enjoined from enforcing any obligation to pay in any contract, deed of trust, or note held by these defendants and entered into between any purchaser and any defendant in connection with purchases of lots at Lake Monticello.

8. No later than thirty (30) days following the entry of this Order, defendants Peterson, Kujawski, Marley, and Costenbader, jointly and severally, shall be, and they hereby are, ordered to make a deposit of one hundred thousand dollars ($100,000) with the Department as an initial payment toward the full amount due.

9. No later than ninety (90) days following the entry of this Order, defendants Peterson, Kujawski, Marley, and Costenbader, jointly and severally, shall be, and they hereby are, ordered to pay to the Department the full amount due.

10. If full payment is not submitted to the Department within ninety (90) days, defendants Peterson, Kujawski, Marley, and Costenbader, jointly and severally, shall be, and they hereby are, ordered to continue to make payments until the entire amount due is satisfied, and interest shall accrue on any unpaid amount at the Treasury rate until the amount due is paid in full. Defendants Peterson, Kujawski, Marley, and Costenbader shall make payments according to the following formula: each year for the seven (7) years from calendar year 1994 through 2001, each defendant shall remit by May 15 of the following year 25% of the net amount of that federal income tax return less any federal, state, and local income taxes paid for that year. If, at the end of seven years the defendants have not satisfied the full amount of the judgment, the defendants shall remain jointly and severally liable for the remainder and shall continue to make payments according to the above formula until the judgment is satisfied in full, and interest

shall continue to accrue on any unpaid amount at the Treasury rate until paid.

11. Defendants Peterson, Kujawski, Marley, and Costenbader shall be, and they hereby are, ordered to file an affidavit with the Department beginning thirty (30) days from the entry of this Order and continuing annually until full restitution has been made as described above, containing the following information: (a) all assets and liabilities as of the date that the affidavit is filed; (b) current business and home addresses and telephone numbers; (c) salary earned during each of the preceding twelve (12) months; (d) all income other than salary received during each of the preceding twelve (12) months; and (e) all bank accounts, including names of the banks and branches, account numbers, and current balances.

12. The asset freeze and sequestration imposed by the Order entered on February 14, 1990 shall be, and it hereby is, reinstated pursuant to the same terms contained therein.

13. This court's Interim Judgment Order entered on April 22, 1992 shall be, and it hereby is, superseded by this Final Judgment Order.

14. This case shall be, and it hereby is, dismissed and stricken from the docket of the court.

The Clerk of the Court is hereby directed to send a certified copy of this Order to all counsel of record and to Magistrate Judge Crigler.

ENTERED: /S/James H. Michael, Jr.
Judge
September 15, 1994
Date

UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

No. 94-2357
CA-89-42-C

U.S. DEPARTMENT OF HOUSING
& URBAN DEVELOPMENT
Plaintiff - Appellee

v.

COST CONTROL MARKETING & SALES MANAGEMENT OF VIRGINIA, INCORPORATED; WILLIAM P. PETERSON; ARTHUR KUJAWSKI; RICHARD R. COSTENBADER; JAMES M. MARLEY

Defendants - Appellants

and

THORNTON BYRON; STUART GUSKIND; EARL HISSOM; MONTICELLO DEVELOPMENT

Defendants

Entered November 3, 1995

On Petition for Rehearing with Suggestion for Rehearing In Banc

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The appellants' petition for rehearing and suggestion for rehearing in banc were submitted to this Court. As no member of this Court or the panel requested a poll on the suggestion for rehearing in banc, and

As the panel considered the petition for rehearing and is of the opinion that it should be denied,

IT IS ORDERED that the petition for rehearing and suggestion for rehearing in banc are denied.

For the Court,

/s/ Bert M. Montague
CLERK

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Re: 94-2357 HUD v. Cost Control
CA - 89-42-C

Dear Counsel:

Enclosed is a copy of an order filed in this case.

Yours truly,
BERT M. MONTAGUE
Clerk

By: /s/ Barbara H. Rowe
Deputy Clerk

Enclosure
cc: Morgan E. Scott Jr.

IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF VIRGINIA
CHARLOTTESVILLE DIVISION

JACK KEMP, Secretary
of Housing and Urban
Development,

Plaintiff

v.

COST CONTROL MARKETING
AND SALES MANAGEMENT
OF VIRGINIA, INC., a
Virginia Corporation,

and

WILLIAM P. PETERSON, individually
and in his capacity as President
of Cost Control Marketing and
Sales Management of Virginia, Inc.,

and

ARTHUR KUJAWSKI, individually and
in his capacity as Vice President
of Cost Control Marketing and
Sales Management of Virginia, Inc.,

and

RICHARD R. COSTENBADER, individually and
in his capacity as Chief Executive Officer
of Cost Control Marketing and Sales
Management of Virginia, Inc.,

and

JAMES M. MARLEY, individually and in his capacity as Secretary / Treasurer of Cost Control Marketing and Sales Management of Virginia, Inc.,

and

THORNTON BYRON, individually and as agent for Cost Control Marketing and Sales Management of Virginia, Inc.,

and

STUART GUSKIND, individually and as agent for Cost Control Marketing and Sales Management of Virginia, Inc.,

and

EARL HISSOM, individually and as agent for Cost Control Marketing and Sales Management of Virginia, Inc.,

and

MONTICELLO DEVELOPMENT CORPORATION, a Virginia Corporation,

Defendants.

Filed November 15, 1989

COMPLAINT

Plaintiff Jack Kemp, the Secretary (the "Secretary') of Housing and Urban Development ("HUD"), by his attorneys, brings this civil action for injunctive and equitable relief, and alleges as follows:

JURISDICTION AND VENUE

1. This action arises under the Interstate Land Sales Full Disclosure Act ("the Act" or "Land Sales Act"), as amended, 15 U.S.C. §1701 et seq. (1982). This Court has jurisdiction pursuant to 15 U.S.C. §§1714(a), 1719, and 29 U.S.C. § 1345.

2. Venue in the Western District of Virginia pursuant to 15 U.S.C. §1719 (1982) and 28 U.S.C. §1391(b) (1982).

PARTIES

3. Plaintiff Jack Kemp is the Secretary of Housing and Urban Development and is authorized by 15 U.S.C. §1714(a) to enforce the Act in his official capacity.

4. Defendant Cost Control Marketing and Sales Management of Virginia, Inc. ("CCMV") is a corporation organized under the laws if the Commonwealth of Virginia and is engaged in the purchase, marketing, and sale of lots at Lake Monticello, Fluvanna County, Virginia, in its own name and under the name "Jefferson Country Model Village World."

5. Defendant William P. Peterson, who is sued in both his individual and corporate capacities, is and at all times relevant to this action was President of Cost Control Marketing and Sales Management of Virginia, Inc.

6. Defendant Arthur Kujawski, who is sued in both his individual and corporate capacities, is and at all times relevant to this action was Vice President of Cost Control Marketing and Sales Management of Virginia, Inc.

7. Defendant James M. Marley, who is sued in both his individual and corporate capacities, is and at all times relevant to this action was Secretary and Treasurer of Cost Control Marketing and Sales Management of Virginia, Inc.

8. Defendant Richard R. Costenbader, who is sued in both his individual and corporate capacities, is and during the time relevant to this action was Chief Executive Officer of Cost Control Marketing and Sales Management of Virginia, Inc.

9. Defendants Thornton Byron, Stuart Guskind, and Earl Hissom during the time relevant to this action acted as salespersons for CCMV in the sale of lots at Lake Monticello.

10. Defendants CCMV, Peterson, Kujawski, Marley, and Costenbader during the time relevant to this action have sold or offered to sell, directly or indirectly, lots in the Lake Monticello subdivision located in Fluvanna County, Virginia. Each of these defendants is therefore a "developer" as defined in 15 U.S.C. §1701(5) (1982).

11. Defendants Byron, Guskind, and Hissom are salespersons who during the time relevant to this action sold or offered to sell lots in the Lake Monticello subdivision on behalf of CCMV. Each of these defendants is therefore an "agent" as defined in 15 U.S.C. §1701 (6) (1982).

12. Defendants CCMV, Peterson, Kujawski, Marely, Costenbader, Byron, Guskind, and Hissom shall be hereafter referred to collectively as "CCMV defendants."

13. Defendant Monticello Development Corporation ("MDC") is a corporation organized under the laws of the Commonwealth of Virginia. MDC at all times relevant to this action aided and abetted CCMV, its officers, and agents in violating the sales practices provisions of the ACT, 15 U.S.C. § 1702(b) (1982).

14. The Act, at 15 U.S.C. §1703(a)(1) (1982), makes it unlawful for any developer or agent, directly or indirectly, with respect to the sale or lease of any lot not exempt under 15 U.S.C. § 1702 (1982), to make use of the mails or any means or instruments of transportation or communication in interstate commerce to sell or lease any lot unless: (A) a Statement of Record with respect to the lot is in effect in accordance with 15 U.S.C. § 1706 (1982), and (B) a printed Property Report, meeting the requirements of 15 U.S.C. § 1707 (1982), has been furnished to the purchaser or lessee in advance or the signing of any contract or agreement for sale or lease by the purchasers.

15. The Act, at 15 U.S.C. §1704(a) (1982), provides that a subdivision may be registered by filing with the Secretary a Statement of Record, meeting the requirements of the Act and such rules and regulations as may be prescribed by the Secretary. According to 15 U.S.C. §1707(a) (1982), a Property Report relating to the lots in a subdivision shall provide as much of the

information contained in the Statement of Record as the Secretary may deem necessary and such other information as the Secretary may by rules or regulations require.

16. The Act, at 15 U.S.C. § 1703(a) (2) (1982), makes it unlawful for any developer or agent, directly or indirectly, with respect to the sale or lease of, or offer to sell or lease, any lot not exempt under 15 U.S.C. § 1702(a) (1982), to make use of the mails or any means or instruments or transportation or communication in intestate commerce to: (1) obtain money or property by means of any untrue statement of a material fact, or any omission to state a material fact necessary in order to make the statements made not misleading, with respect to any information pertinent to the lot or subdivision, 15 U.S.C. § 1703(a) (2) (B); see also 24 C.F.R. § 1715.15; ir (2) engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon a purchaser, 15 U.S.C. § 1703 (a) (2) (C) (1982).

17. The Act, at 15 U.S.C. § 1714(a) (1982), authorizes the Secretary to bring an action against any person who is engaged or about to engage in any acts or practices which violate the Act or its regulations. That section further provides that "upon a proper showing, a permanent or temporary injunction or restraining order shall be granted without bond." The Act, at 15 U.S.C. § 1713 (1982), states that the rights and remedies provided by the Act shall be in addition to any and all other rights and remedies that may exist at law or in equity.

The regulations implementing the Act are codified at 24 C.F.R. §§ 1710 et seq.

Count I

VIOLATION OF THE REGISTRATION REQUIREMENTS

18. Plaintiff incorporates and realleges the allegations set forth in Paragraphs 1 - 17 above.

19. CCMV owns certain real property in an area known as Lake Monticello, located in Fluvanna County, Virginia. This property ("Lake Monticello") is divided into more than 100 lots for the purpose of sale as a part of a common promotional plan. Lake Monticello therefore constitutes a "subdivision" as defined in 15 U.S.C. § 171(3) (1982).

20. Since approximately January 1, 1987, CCMV defendants have been and are, directly or indirectly, making use of means or instruments of transportation or communication in interstate commerce and of the mails to offer to sell and to sell lots at Lake Monticello. This includes, but is not limited to, the use of the United States mails, of telephones, including interstate use of "800" numbers, and of advertising in newspapers with interstate circulation.

21. The offers to sell and the selling of lots at Lake Monticello by CCMV defendants do not qualify for any exemption under the Act, 15 U.S.C. § 1702 (1982).

22. There is not and has not been at times relevant to this action a Statement of record in effect for Lake Monticello on file with the HUD Office of Interstate Land Sales. Registration prior to sale is required by 15 U.S.C. § 1703 (a)(1)(A) (1982). Nonetheless, since approximately January 1, 1987, CCMV

defendants, directly or indirectly, have sold or have offered to sell lots at Lake Monticello and continue to do so when there is no Statement of Record in effect for such lots.

23. Based upon the foregoing, CCMV defendants have sold or offered for sale and, unless enjoined, will continue to sell or offer for sale lots at Lake Monticello in violation of 15 U.S.C. § 1703(a)(1)(A) (1982) and its implementing regulations. The injuctive and other equitable relief requested herein is, therefore, both appropriate and necessary.

Count II

VIOLATIONS OF DISCLOSURE REQUIREMENTS

24. Plaintiff incorporates and realleges the allegations set forth in Paragraph 1-23 above.

25. CCMV defendants, directly or indirectly, have sold lots in the Lake Monticello subdivision without providing purchasers with printed Property Reports meeting the requirements of 15 U.S.C. § 1707 (1982) and its implementing regulations, in advance of the signing of their lot sales agreements.

26. Based upon the foregoing, CCMV defendants have sold lots at Lake Monticello in violation of 15 U.S.C. § 1703(a)(1)(B) (1982) and its implementing regulations and, unless enjoined, will continue to sell or offer to sell lots at Lake Monticello in violation of 15 U.S.C. § 1703(a)(1)(B) (1982) and its implementing regulations. The injunctive and other equitable relief

requested herein is, therefore, appropriate and necessary.

Count III

VIOLATIONS OF THE SALES PRACTICES PROVISIONS OF THE ACT

27. Plaintiff incorporates herein and realleges the allegations set forth in Paragraphs 1-26 above.

28. In the course of selling or offering to sell lots at Lake Monticello, defendants, directly or indirectly, have obtained and will continue to obtain money by means of untrue statements of material facts and omissions to state material facts and omissions to state material facts necessary in order to make the statements made (in light of the circumstances in which they were made and within the context of the overall offer and sale) not misleading with respect to information pertinent to individual lots or to Lake Monticello as a whole. Further, defendants have engaged in and will continue to engage in transactions, practices and courses of business which operate or would operate as a fraud or deceit upon purchasers. Defendants' conduct includes, but is not limited to, the following actions:

(a) failing to furnish each purchaser with a printed Property Report in advance of the purchaser's signing a contract or agreement, in violation of 15 U.S.C. § 1703(a)(1)(B) and 24 C.F.R. § 1715.15(d);

(b) using misleading practices, devices or representations which deny purchasers cancellation or refund rights or privileges granted to purchasers, in

violation of 15 U.S.C. §1703(a)(2)(B) and (C) and 24 C.F.R. § 1715.20(d), in that CCMV defendants omit to state or misrepresent to purchasers revocation rights available under 15 U.S.C. §§ 1703(b) and (c) and fail to honor purchasers' attempted revocations;

(c)violating the requirements of 15 U.S.C. §§ 1703(a)(2)(B) and (C) and 24 C.F.R. §1715.20(h) by using, as a sales inducement, representations that the lots in Lake Monticello have a good investment potential or will increase in value when it cannot be and is not established in writing that: (1) comparable lots in the subdivision have, in fact, been resold by their owners on the open market at a profit, or (2) there is a factual basis for the represented future increase in value and the factual basis is certain, and (3) the sales price of the offered lot does not already reflect the anticipated increase in value due to any promised facilities or amenities. In fact, there is no local market for such lots even at the prices for which the CCMV defendants sold such lots;

(d)leading prospective purchasers to believe through its advertising that CCMV offers house-lot packages at Lake Monticello. In fact, CCMV only sells lots at inflated prices;

(e)representing to prospective purchasers that they can buy a house and lot in Lake Monticello by making a low down payment and making payments on a fixed rate mortgage for the total price of the house and lot, when, in fact, purchasers are not able to make a single down payment and obtain the represented financing for the house-lot package;

(f) inducing purchasers to sign high interest rate notes for their lot purchases by telling the purchasers that the debt for their lot purchases can later be combined with the debt on their home construction loans at a lower interest rate, when, in fact, purchasers are unable to so restructure their debt at lower interest rates;

(g) representing, as a sales inducement, that CCMV, or an agent of CCMV, will manage a rental company for rentals of homes built on Lake Monticello lots, when, in fact, no such rental management company has operated as of this date;

(h) representing, in violation of 24 C.F.R. § 1715.25(c), as a sales inducement, that purchasers can rent homes built on their lots on a short term basis when, in fact, the restrictions placed on the rentals of homes by the Lake Monticello Property Owners Association prohibit short term rentals of homes;

(i) using misleading practices, devices or representations which lead potential purchasers to believe that CCMV is and has been the only entity selling lots at lake Monticello, when, in fact, CCMV is not the exclusive seller of lots at Lake Monticello and other sellers are offering and have offered lots for lower prices;

(j) representing to potential purchasers that the only lots at Lake Monticello available for purchase near recreational facilities as advertised, such as the lake, golf course, or beaches, are available only at prices much higher than prices advertised. In fact, such lots are available for purchase at substantially lower

prices from other owners of lots at Lake Monticello. Indeed, on several occasions, CCMV defendants informed purchasers that no lake front property was available despite advertisements indicating such availability;

(k) creating, in violation of 24 C.F.R. § 1715.25(k), a high pressure sales environment by repeatedly announcing over radio airwaves that lots were being sold or repeatedly announcing the same lot being sold when, upon information and belief, such sales had not occurred;

(l) using, in violation of 24 C.F.R. § 1715.25(m), a discount certificate entitled "Model Homesite Agreement" as an enticement to purchase a lot on the same day as the tour, when in fact, such a "discount certificate" is regularly used;

(m) requiring purchasers to pay $800, purportedly for closing costs, when in fact that charge bears no relationship to the actual closing costs incurred by CCMV; and

(n) inducing each purchaser who buys a lot from CCMV to sigh a $1,500 note payable to MDC purportedly for causing utility services to be extended to the lot. Upon information and belief, MDC is not entitled to collect the $1,500 fee on most of the lots sold by CCMV in Lake Monticello.

29. In violation of 15 U.S.C. § 1703(b) and 24 C.F.R. § 1715.2, CCMV defendants have used contracts and agreements (including promissory notes) for lot sales at Lake Monticello which fail clearly to provide that the purchaser has until at least midnight of the seventh day following the signing of the contract or agreement to revoke such contract or agreement.

30. In violation of 15 U.S.C. § 1703(c) and 24 C.F.R. § 1715.3, CCMV defendants have used contracts and agreements (including promissory notes) which do not clearly provide that purchasers have the right to revoke such contracts and agreements within tow years from the date of signing the contract or agreement if the purchaser was not given the required Property Report before signing the contract or agreement.

31. Based upon the foregoing, CCMV defendants and MDC have violated and, unless enjoined, will continue to violate 15 U.S.C. §§ 1703(a)(2)(B) and (C), 1703(c) (1982) and the Act's implementing regulations. Injunctive and other equitable relief is, therefore, both appropriate and necessary.

RELIEF REQUESTED

I. Preliminary Injunction

Plaintiff prays that, pending a final determination of this action, the Court:

A. Issue a preliminary injunction restraining CCMV defendants, and their officers, agents and employees, as well as all individuals and entities acting in concert or participation with any defendants, from:

(1) violating the Act and its implementing rules and regulations including, but not limited to:

(a) offering to sell or selling lots at Lake Monticello while there are no Statements of Record or Property Reports in effect with respect to the

subdivision or failing to provide purchasers with Property Reports prior to the signing of their lot sales contract;

(b) engaging in other activities or conduct in violation of the Act as set forth in Counts I-III;

(2) assigning or transferring the right to receive payments arising from the sale of lots in the subdivisions;

B. Issue a preliminary injunction restraining defendants CCMV, Peterson, Marley, Kujawski, and Costenbader, their officers, agents and employees, as well as all individuals and entities acting in concert or participation with them, from transferring or disposing of corporate or personal monies or other assets except for payment of reasonable living expenses and expenses in the normal course of business;

C. Issue an order requiring that all monies received by defendants CCMV, Peterson, Kujawski, Marley and Costenbader from person who bought lots at Lake Monticello from CCMV (Lake Monticello purchasers) be placed in an escrow account with an independent institution having trust power under the supervision of the Court pending final disposition of the action.

II. Permanent Injunction

Plaintiff prays that, upon a final adjudication of the merits, the Court,

A. Issue a permanent injunction restraining MDC, CCMV defendants, and their

officers, agents and employees, as well as all individuals and entities acting in concert or participation with any defendant, from violating the act and its implementing rules and regulations, including, but not limited to:

(1) offering to sell or selling lots Lake Monticello while there are statements of Record or Property Reports in effect with respect to the subdivision or failing to provide purchasers with Property Reports prior to the signing of their lot sale contracts; and

(2) engaging in other activities or conduct in violation of the Act as set forth in Counts I through III;

B. Order, pursuant to its equity powers, restitution of all monies paid to all defendants by Lake Monticello purchasers in connection with their purchases (including payments to MDC), rescission of all contracts, deeds of trust and notes, and/or disgorgement of all monies obtained by defendants in violation of the Act and delivery of such monies to a trustee appointed by the Court;

C. Appoint a trustee with authority to receive monies from defendants and to distribute them in a proper and equitable manner in accordance with the Court's instructions;

D. Order, pursuant to its equity powers, that MDC be enjoined from foreclosing upon the deeds of trust granted by purchasers of lots from CCMV, and from enforcing the

underlying noes and from transferring the notes to any entity other than CCMV;

E. Order such other and further relief as this Court may deem just and proper.

Respectfully submitted,

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Assistant Attorney General

JOHN P. ALDERMAN
United States Attorney

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IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF VIRGINIA
CHARLOTTESVILLE DIVISION

JACK KEMP, Secretary of Housing
and Urban Development,

Plaintiff,

v.

COST CONTROL MARKETING AND SALES MANAGEMENT
OF VIRGINIA, INC., a Virginia Corporation,
et al.,

Defendants.

Civil Action No. 89-0042-C

Filed January 14, 1992

DECLARATION OF ROGER G. HENDERSON

1. I am the Director of the Interstate Land Sales Registration Division, otherwise known as "OILSR", of the United States Department of Housing and Urban Development ("HUD"). In this capacity, I have knowledge of the day-to-day operations of OILSR and the enforcement of the Interstate Land Sales Full Disclosure Act ("the Act"), 15 U.S.C. §§ 1701 et seq. My staff and I are responsible for investigating possible violations of the Act, gathering and analyzing evidence during the litigation process, processing consumer complaints, and conducting negotiations with developers charged with violations of the Act.

2. In December, 1991, my office sent questionnaires to the 466 purchasers known to

us who purchased lots from the defendants at the Lake Monticello subdivision in Fluvanna County, Virginia. We obtained the names and addresses of such 466 purchasers from the files of the defendants during discovery. However, it is possible that additional individuals unknown to us also purchased lots from the defendants at the Lake Monticello subdivision. The purpose of the questionnaires was to obtain actual figures from purchasers concerning the prices for the lots purchased from the defendants and the value of such lots.

3. Attached to this declaration as Exhibit A are samples of the Questionnaires sent to the purchasers. These questionnaires ask for such information as the amount of the purchase price of the purchaser's lot and the valuation of the lot on the most recent tax assessment. The difference between what the purchasers paid and the value of what they received.

4. My office contacted the Office of the Commissioner of the Revenue for Fluvanna County to obtain information as to what value the most recent tax assessment represents. My office was informed that the tax assessment represents 100% of assessed value, and that the most recent tax assessment is based upon an assessment done in 1987. My office's investigation indicated that the defendants sold these lots to the purchasers during the 1987 through 1989 time period, and that the defendants did not make improvements to these lots prior to sale. Therefore, the most recent tax assessment of each lot is a reasonable indication of the value of the lot at the time of sale. Furthermore, the assessed value is undoubtedly greater than

the price the defendants paid for the lots, that is, their acquisition price. Such assessed value figures are readily attainable from Fluvanna County.

5. This office received complete figures on 258 questionnaires. In this office's experience in sending out questionnaires, the receipt back of 258 out of 466 questionnaires sent represents an extremely high rate of return. The majority of questionnaires which were not returned were not returned because we did not have current addresses for the purchasers.

6. A preliminary review of the questionnaires shows that 258 purchasers at Lake Monticello paid the defendants a total of $6,842,275 for land which was valued at only $2,054,300. The average sale price for these purchasers was 26,520. The average assessed value of the property for these purchasers was $7962. Taking these averages of the amount each purchaser paid and of the assessed value of each lot sold, this office has preliminary determined that the total amount paid to the defendants for the 466 lots would be approximately $12,358,528, and that the total assessed value for the 466 lots would be approximately $3,710,480. Therefore, it is reasonable to conclude that the difference between what the 466 purchasers paid and the value of what they received would be approximately $8,658,048.

I declare under penalty of perjury that the foregoing is true and correct.

Executed this 13th day of January, 1992.

/s/ROGER G. HENDERSON
ROGER G. HENDERSON

IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF VIRGINIA
CHARLOTTESVILLE DIVISION

HENRY G. CISNEROS, SECRETARY
OF THE DEPARTMENT OF HOUSING
AND URBAN DEVELOPMENT

Plaintiff,

v.

COST CONTROL MARKETING AND
SALES MANAGEMENT OF
VIRGINIA, INC., ET AL.,

Defendants.

Filed August 12, 1994

OBJECTIONS TO REPORT AND RECOMMENDATION SUBMITTED BY B. WAUGH CRIGLER, U.S. MAGISTRATE UNDER DATE OF JULY 27, 1994

NOW COME Defendants William Peterson, Arthur Kujawski, James Marley, and Richard Costenbader in their official capacity as officers of Cost Control Marketing and Sales Management of Virginia, Inc., by their attorney of record, Francis T. Eck, and object to the report and recommendation filed by the United States Magistrate Judge B. Waugh Crigler on July 27, 1994 as follows:

1. Those objections filed by Marshall E. Anders, Esq. co-counsel for defendants dated August 5, 1994 are incorporated herein by reference.

2. This Court ordered a stay in the collateral June P. Bailey, et al. vs. Cost Control Marketing and Sales Management of Virginia (No. 89-0041-C) case due to the multiple bankruptcies of several defendants. Such stay also included any case to which these individuals were a party, and specifically the instant case. With the stay in effect, it was error for the plaintiff to proceed with discovery. Defendants were within their legal right to refuse to answer any discovery requests.

3. With the stay in effect, defendants were themselves without authority to proceed further. Therefore, the ability to address the amount of disgorgement was lacking. It was not incumbent on such defendants to inquire on the issue of disgorgement notwithstanding any suggestion of the Magistrate Judge to the contrary.

4. Any judgment entered by this Court must be reduced by the amount or benefit each lot purchaser received occasioned by the settlement and dismissal of the Bailey case.

Respectfully submitted,

William Peterson
Arthur Kujawski
James Marley
Richard Costenbader

By: /s/Francis T. Eck

Francis T. Eck
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16 South Second Street
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I hereby certify that I mailed a true and exact copy hereof on the 10th day of August, 1994 to:

Marshall E. Anders, Esq.
802 Main Street
Stroudsberg, PA 18360
(717) 424 - 6661
and
Eric Johnson Mahr, Esq.
U.S. Department of Justice
901 E. Street, NW - Room 941
Washington, DC 20530

/s/ Francis T. Eck
Francis T. Eck

(3)

Supreme Court, U.S.
FILED
APR 3 1996
CLERK

No. 95-1233

In the Supreme Court of the United States

OCTOBER TERM, 1995

COST CONTROL MARKETING & SALES MANAGEMENT OF VIRGINIA, INC., ET AL., PETITIONERS

v.

HENRY G. CISNEROS, SECRETARY OF HOUSING AND URBAN DEVELOPMENT

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

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21 pp

QUESTIONS PRESENTED

1. Whether petitioner Cost Control Marketing and Sales Management of Virginia, Inc., which engaged in the interstate marketing and sale of land, is a "developer" within the meaning of the Interstate Land Sales Full Disclosure Act, 15 U.S.C. 1701(5).

2. Whether the disgorgement ordered by the district court, payable to the Secretary of Housing and Urban Development, is exempted from the discharge provisions of the Bankruptcy Code under 11 U.S.C. 523(a)(7), which exempts from discharge any "fine, penalty, or forfeiture" that is payable "to and for the benefit of a governmental unit," and is "not compensation for actual pecuniary loss."

3. Whether the district court properly ordered disgorgement to respondent based on evidence in affidavits presented by respondent that was not controverted by any petitioner.

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In the Supreme Court of the United States

OCTOBER TERM, 1995

No. 95-1233

COST CONTROL MARKETING & SALES MANAGEMENT OF VIRGINIA, INC., ET AL., PETITIONERS

v.

HENRY G. CISNEROS, SECRETARY OF HOUSING AND URBAN DEVELOPMENT

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the court of appeals from which review is sought (Pet. App. A1-A15), affirming final judgment for respondent, is reported at 64 F.3d 920. The opinion and order of the district court directing the entry of final judgment (Pet. App. A62-A72) are reported at 862 F. Supp. 1531. The report of the magistrate judge recommending the entry of final judgment for respondent (Pet. App. A53-A61) is unreported.

A prior opinion of the court of appeals (Pet. App. A22-A30) is reported at 940 F.2d 110. The opinion and order of the district court directing an interim final judgment (Pet. App. A31-A50) are reported at 790 F. Supp. 1275. The order of the district court entering a preliminary injunction (Pet. App. A16-A21) is unreported.

JURISDICTION

The judgment of the court of appeals was entered on September 8, 1995. A petition for rehearing was denied on November 3, 1995. Pet. App. A77-A78. The petition for a writ of certiorari was filed on January 31, 1996. This Court's jurisdiction is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. Petitioner Cost Control Marketing and Sales Management of Virginia, Inc. (CCMV) is a Virginia corporation formed for the sole purpose of purchasing, marketing, and selling unimproved lots of land in Lake Monticello, Virginia, a subdivision of over 4,500 lots. Pet. App. A3, A23. CCMV is wholly owned by three of its officers, petitioners Peterson, Kujawski, and Marley. *Id.* at A3. Petitioner Costenbader is Chief Executive Officer of CCMV. *Ibid.*

Between 1986 and 1989, CCMV purchased over 900 unimproved lots in the Lake Monticello subdivision, and then marketed those lots to prospective purchasers in Washington, New York, and elsewhere. Pet. App. A3. By the end of 1989, CCMV had sold 585 lots. *Ibid.* None of CCMV's sales complied with the Interstate Land Sales Full Disclosure Act (ILSFDA or the Act), 15 U.S.C. 1701 *et seq.*, which, like the federal securities laws, imposes certain registration and disclosure requirements and prohibits fraudulent

and misleading sales practices. See generally *Flint Ridge Development Co.* v. *Scenic Rivers Ass'n*, 426 U.S. 776, 778 (1976); *Cost Control Mktg. & Management, Inc.* v. *Pierce*, 848 F.2d 47, 48 (3d Cir. 1988).

Under ILSFDA, developers and agents may not use any means of interstate commerce or the mails to offer or sell lots in a subdivision without registering the property by filing a statement of record with the Department of Housing and Urban Development (HUD). 15 U.S.C. 1703(a)(1)(A) and 1704.[1] Developers and their agents also must furnish a prospective purchaser with a complete and accurate printed disclosure statement, known as a "property report," prior to the execution of any sales contract. 15 U.S.C. 1703(a)(1)(B) and 1707. Purchasers may revoke their contracts within two years if they were not provided property reports prior to signing the contracts. 15 U.S.C. 1703(c). The Act prohibits misleading sales practices and mandates certain sales practices to inform and protect consumers. 15 U.S.C. 1703(a)(2). The Act also makes it unlawful for any developer or agent to "obtain money or property by means of any untrue statement of a material fact, or any omission to state a material fact." 15 U.S.C. 1703(a)(2)(B). Finally, the Act prohibits developers and agents from engaging "in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon a purchaser." 15 U.S.C. 1703(a)(2)(C).

---

[1] The Act defines a "developer" as "any person who, directly or indirectly, sells or leases, or offers to sell or lease, or advertises for sale or lease any lots in a subdivision." 15 U.S.C. 1701(5). An "agent" is "any person who represents, or acts for or on behalf of, a developer in selling or leasing, or offering to sell or lease, any lot or lots in a subdivision." 15 U.S.C. 1701(6).

CCMV failed to register its lots, failed to provide required property reports to purchasers, failed to inform purchasers of their two-year right to rescind, and refused to rescind sales upon purchasers' requests. Pet. App. A4. CCMV also used high-pressure, misleading marketing techniques. *Ibid.* As a result of these unlawful practices, CCMV was able to sell lots at over three times their assessed value. *Ibid.*

2. On November 15, 1989, HUD filed suit against petitioners in district court, alleging that petitioners had violated the registration and disclosure provisions of ILSFDA, and had engaged in sales practices prohibited by the Act, including overcharging for closing costs, misleading advertising, and misinforming purchasers regarding their revocation rights. Pet. App. A4, A24. HUD requested injunctive relief and disgorgement of petitioners' illegal profits. *Id.* at A4, A93-A96. On February 14, 1990, the district court granted a preliminary injunction against future violations of the Act by petitioners and froze the individual petitioners' assets. *Id.* at A16-A21.

On interlocutory appeal, the court of appeals affirmed the preliminary injunction, but remanded the case to the district court for factual findings under Federal Rule of Civil Procedure 65(d) in connection with the asset freeze. Pet. App. A24. In affirming the issuance of the injunction, the court of appeals rejected petitioners' sole defense to liability, and held that CCMV could be held liable under the Act's definition of "developer" in Section 1701(5), and that the individual petitioners could be held liable as "agents" of CCMV under Section 1701(6). Pet. App. A4, A26-A27.

3. On April 22, 1992, after having granted summary judgment in favor of HUD on all counts, the district court issued an interim judgment order. Pet. App. A31-A50. The court concluded that petitioners' violations constituted "part of a pattern of conduct that suggests a strong propensity to repeat itself in the absence of a permanent injunction." *Id.* at A33. The court found that petitioners "appear to be absolutely unrepentant." *Ibid.* It noted that petitioners had been twice held in contempt by the magistrate judge for defying the court's orders, and had otherwise made it clear to the court that they did "not feel bound by the orders of this court (or by the law)." *Id.* at A33-A34. Accordingly, the court permanently enjoined petitioners from enforcing any obligation to pay in connection with their sale of lots at Lake Monticello. *Id.* at A47.

In its interim judgment order, the district court also considered HUD's request for disgorgement of petitioners' illegal profits, and found that HUD's proposed disgorgement figure of $8,648,048 was a "reasonable approximation" of the amount of profits petitioners received from their unlawful activities. Pet. App. A38, A43-A45. The court stated that, at the appropriate time after discovery, it would calculate the precise amount of profits that were causally connected to the violations and had been passed through CCMV to each individual petitioner. *Ibid.*

On September 1, 1992, three of the four individual petitioners in this case (Peterson, Marley, and Costenbader) filed individual bankruptcy petitions under Chapter 7 of the Bankruptcy Code. Pet. App. A6. On September 4, 1992, pursuant to the interim judgment order, HUD served all four individual petitioners with discovery requests, seeking information

about the profits received from their illegal sales, their current assets and liabilities, and transactions with their relatives. *Id.* at A6-A7. None of the petitioners responded to HUD's interrogatories. *Id.* at A7-A9. Moreover, none of the petitioners submitted any evidence to the court challenging HUD's proposed disgorgement relief of $8,648,048, or demonstrating that they should not each incur continuing joint and several liability for that entire amount. *Ibid.*

4. On September 15, 1994, the district court entered final judgment against petitioners. Pet. App. A62-A72. The court rejected petitioners' contention that their bankruptcy petitions prevented HUD's enforcement action from going forward. It held that, because this action was brought by HUD to enforce its regulatory powers, it is exempt from the automatic stay provisions of the Bankruptcy Code pursuant to 11 U.S.C. 362(b)(4). It also held that the disgorgement relief in this case is excepted from the Bankruptcy Code's discharge of debts under 11 U.S.C. 523(a)(7), as a "fine, penalty, or forfeiture" payable "to and for the benefit of a governmental unit" that is "not compensation for actual pecuniary loss." Pet. App. A64-A68. The district court also noted that, after more than 27 months, petitioners had failed to rebut or even challenge HUD's figure of $8,648,048 as a reasonable approximation of the illegal profits that should be disgorged. Pet. App. A70. Accordingly, it entered judgment against petitioners in that amount, payable to the Secretary of HUD, and it permanently enjoined petitioners from violating the Act or enforcing any obligations against purchasers of Lake Monticello lots. *Id.* at A73-A76.

5. The court of appeals affirmed. Pet. App. A1-A15. It first held, as it had on the interlocutory appeal, that CCMV is a "developer" under Section 1701(5). Pet. App. A8. It then rejected petitioners' challenge to the sufficiency of HUD's proof in support of the disgorgement order, noting that HUD's evidence was "absolutely uncontradicted" by petitioners. *Id.* at A10. The court reasoned that the Declaration of Roger Henderson, Director of HUD's Interstate Land Sales Registration Division, upon which the district court's award was based in part, served "as a summary of voluminous evidence" and that "[s]omething like it would doubtless have been permitted at a trial of this case." *Ibid.* The court also noted that the Henderson Declaration was corroborated by other evidence of record, including the sworn declarations of 11 lot purchasers. It concluded that HUD had carried its burden of coming forward with a "reasonable approximation of the illegal profits." *Id.* at A10-A11 (citing *SEC* v. *First City Financial Corp.*, 890 F.2d 1215 (D.C. Cir. 1989)).

The court of appeals also agreed with the district court that the Bankruptcy Code does not shield petitioners from the district court's disgorgement order. Pet. App. A12-A14. It ruled that this enforcement action brought by HUD is exempted from the automatic stay provision of the Code by 11 U.S.C. 362(b)(4), which exempts "the commencement or continuation of an action or proceeding by a governmental unit to enforce such governmental unit's police or regulatory power." See Pet. App. A12-A13. It also ruled that, under 11 U.S.C. 523(a)(7), the disgorgement award is excluded from the discharge of petitioners' debts as "a fine, penalty, or forfeiture payable to and for the benefit of a governmental unit,

and * * * not compensation for actual pecuniary loss." See Pet. App. A13-A14.

ARGUMENT

1. Petitioner CCMV contends (Pet. 7-14) that it was not a "developer" covered by ILSFDA, 15 U.S.C. 1701(5), because it was merely a seller of already developed property (Pet. 8). That contention is incorrect. The Act defines a "developer" as "any person who, directly or indirectly, sells or leases, or offers to sell or lease, or advertises for sale or lease any lots in a subdivision." 15 U.S.C. 1701(5). Although the Act may have been directed in large part at those who market undeveloped property, it is not limited to those sellers, and its definition of "developer" does not distinguish between original developers and subsequent large-scale resellers of developed "lots in a subdivision."

As the lower court observed in rejecting a similar argument in an earlier case, "[t]o exclude all but the original developer from the purview of the Act would clearly circumvent its intent by permitting developers to simply transfer land to separate entities before being sold to the public." *Olsen* v. *Lake Country, Inc.*, 955 F.2d 203, 205 (4th Cir. 1991), cert. denied, 503 U.S. 972 (1992). Moreover, in many situations, it may be unclear whether a subdivision has in fact been "developed"; in *Olsen*, for example, "there were serious questions concerning the ability of the water supply and sewer system to service all homes in the subdivision." *Id.* at 206. In addition, under HUD regulations implementing the Act (see 15 U.S.C. 1707), the "property report," or disclosure statement to prospective customers, required of developers must set forth important information that

does not turn on the developed status of the subdivision, including information about encumbrances, utility connections, and the financial situtation of the developer. See 24 C.F.R. 1710.100 *et seq.* Contrary to CCMV's contention (Pet. 8-9), therefore, it is not true that "the potential buyer does not need disclosure of the features of a completed development, for the subdivision in place speaks for itself." See also *Winter* v. *Hollingsworth Properties, Inc.*, 777 F.2d 1444, 1447 (11th Cir. 1985) (noting that ILSFDA is not limited to sales of "raw land" but is applicable "to *all* lots" in a subdivision).[2]

"The general purpose of [ILSFDA] was, of course, to prohibit and punish fraud in * * * land development enterprises * * * and the Act should be interpreted to attain that end. Such an act should be construed 'not technically and restrictively, but flexibly to effectuate its remedial purposes.'" *McCown* v. *Heidler*, 527 F.2d 204, 207 (10th Cir. 1975).[3]

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[2] ILSFDA does not cover sales of *improved* land on which an already completed residential building exists. See 15 U.S.C. 1702(a)(2). This case does not involve that exemption. Also, the registration and disclosure requirements of ILSFDA do not apply to the sale of lots in a subdivision containing fewer than 100 lots, 15 U.S.C. 1702(b)(1), and the Act as a whole does not apply to the sale of lots in a subdivision containing fewer than 25 lots (unless the method of disposition is designed for the purpose of evading the Act), 15 U.S.C. 1702(a)(1).

[3] Although petitioner suggests (Pet. 9) that *McCown* applied an "opposite interpretation" of the Act by considering extenuating facts and circumstances, that case did not involve the question whether ILSFDA applies to sellers of developed lots. *McCown* held that officers and directors of a corporate developer could be held liable under ILSFDA as controlling persons, or aiders and abettors, of the corporate developer. 527 F.2d at 207.

Given the clear language of the Act, its remedial purposes, and the difficulty of drawing a clear line between "developed" and "undeveloped" lots, there is no reason to conclude that Congress intended to exclude sellers of lots like CCMV from the reach of the Act.

The other appellate cases relied on by CCMV (Pet. 9-10) are not to the contrary. In *Bartholomew* v. *Northampton National Bank of Easton*, 584 F.2d 1288 (3d Cir. 1978), the court concluded that a bank that provided financing for a development project was not liable under ILSFDA as an "indirect seller" or aider and abettor of the primary developer. The court reached that conclusion, not because the lots at issue were already developed (they were not), but because the bank did not actively participate in the actual sales of the lots. *Id.* at 1292-1293; see also *Adema* v. *Great Northern Development Co.*, 374 F. Supp. 318 (N.D. Ga. 1973). In *Cumberland Capital Corp.* v. *Harris*, 621 F.2d 246 (6th Cir. 1980), the court held that a bank that occasionally sold lots on which it foreclosed as an outgrowth of its lending activities was not a developer. The court did not emphasize the developed or undeveloped status of the lots, and it noted that arguably the bank fell within the strict definition of "developer." *Id.* at 250. It emphasized, however, that the statutory definition of "subdivision" requires that the lots in a subdivision be sold pursuant to a "common promotional plan," *ibid.*, which was not true of the bank's "involvement in land sales, undertaken only as necessitated by defaulting borrowers, [and] truly 'incidental' in character," *id.* at 249.

2. Petitioners Costenbader, Peterson, and Marley argue (Pet. 14-22) that the Bankruptcy Code's dis-

charge provisions shield them from the district court's disgorgement order. In particular, they take issue with the lower courts' conclusions that the disgorgement order is exempt from discharge because it is "a fine, penalty, or forfeiture payable to and for the benefit of a governmental unit, and is not compensation for actual pecuniary loss." 11 U.S.C. 523(a)(7).

Petitioners contend (Pet. 14-16) that "civil restitution orders" are not exempt from discharge under Section 523(a)(7). In *Kelly* v. *Robinson*, 479 U.S. 36 (1986), this Court held that restitution orders imposed in criminal prosecutions are excepted from discharge under Section 523(a)(7). The Court emphasized that that Section creates "a broad exception for all penal sanctions, whether they be denominated fines, penalties, or forfeitures." 479 U.S. at 51. The Court subsequently made clear that Section 523(a)(7) covers both civil and criminal fines, penalties, and forfeitures. See *Pennsylvania Dep't of Public Welfare* v. *Davenport*, 495 U.S. 552, 561-562 (1990).

The disgorgement at issue in this case is sufficiently penal to be considered a "fine, penalty, or forfeiture," for purposes of Section 523(a)(7), even though it was entered in a civil proceeding.[4] HUD

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[4] Petitioners rely (Pet. 17) on part of the definition of "forfeiture" in *Black's Law Dictionary*. That entry, however, also defines "forfeiture" as the "[l]oss of some property or money because of breach of a legal obligation," without any distinction between the criminal and civil contexts. *Black's Law Dictionary* 650 (6th ed. 1990). The disgorgement order in the instant case is unquestionably a "forfeiture" in the common usage of that term, since the amount disgorged represents the profits on petitioners' land sales that petitioners have been

brought this action against petitioners under 15 U.S.C. 1714(a), which permits such actions when the Secretary believes that any person is engaged in "a violation" of the Act. See Pet. App. A83. And as the magistrate observed (*id.* at A57-A58), "pursuit of the judgment in this case has been driven by a desire to punish [petitioners] for their clear violations of the law and to serve as a deterrent [to violations] of the Act, not by a desire for victim compensation." See also *id.* at A68 (same observation by district court).[5]

The disgorgement order also satisfies the two additional requirements of Section 523(a)(7). The award is indisputably payable "to and for the benefit of a governmental unit," since the order requires that the $8.65 million judgment be paid directly to the Secretary of HUD and places no restrictions on its use by the Secretary. Pet. App. A68, A74. The award is also "not compensation for actual pecuniary loss." As the court of appeals pointed out (*id.* at A14), in the context of Section 523(a)(7), that phrase "refers to the *government's* pecuniary loss." There is no such loss implicated in this case.[6] Moreover, the purpose of the

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required to forfeit as a result of their breach of their legal obligations under the Act.

[5] Petitioners' argument (Pet. 20-21) that HUD should have resorted to the civil penalty provisions of ILSFDA is unavailing. Those provisions did not become effective until December 15, 1989, after the complaint in this action was filed, and their application was expressly prospective. 15 U.S.C. 1717a note.

[6] In *Kelly* v. *Robinson*, *supra*, the Court concluded that a restitution order is not "compensation for actual pecuniary loss" because "[t]he sentence following a criminal conviction necessarily considers the penal and rehabilitative interests of the State." 479 U.S. at 53. Although the Court therefore

disgorgement award is not compensatory, even as it relates to the private victims of petitioners' violations of the law. The purpose of the disgorgement is to ensure that petitioners do not profit from their illegal sales practices; thus, the award is based, not on what the victims lost, but on what petitioners illegally gained, as a result of their violations of the Act.

In re Taite, 76 B.R. 764 (Bankr. C.D. Cal. 1987), the sole case petitioners offer in support of their dischargeability argument (Pet. 20-21), is not to the contrary. The court in *Taite* expressly ordered that the relief awarded "shall be used to reimburse * * * customers for funds they paid to defendants or their assignees." 76 B.R. at 772. As a result, the *Taite* court found that the relief ordered in that case was of the type "primarily intended to compensate victims for their losses," and was, therefore, not exempt under Section 523(a)(7). *Ibid.* *Taite* is inapposite to the award in the instant case, which does not require compensation of petitioners' customers. Moreover, the award in this case was entered principally for the purposes of punishment and deterrence, not compensation of petitioners' customers, and was not based on the amount that those customers lost to petitioners.

3. Finally, petitioners challenge (Pet. 22-29) the sufficiency of the evidence supporting the district court's disgorgement order. That challenge is without merit.

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rejected the argument that the restitution order was intended "'for . . . compensation' of the victim," *ibid.*, it did not hold that Section 523(a)(7) refers to pecuniary loss by a private party, rather than the governmental unit to which the fine, penalty, or forfeiture is directly owed.

Because separating legal from illegal profits precisely can be "a near-impossible task," the courts have recognized that the actual calculation of disgorgement "need only be a reasonable approximation of profits causally connected to the violation." *SEC* v. *First City Financial Corp.*, 890 F.2d 1215, 1231 (D.C. Cir. 1989). In finding that HUD had satisfied its burden of coming forward with a "reasonable approximation" of petitioners' illegal profits, the district court relied in part upon the Declaration of Roger Henderson, Director of HUD's Interstate Land Sales Registration Division, which set forth an approximation of the profits that petitioners derived from their illegal land sales. See Pet. App. A10, A98-A100. The Henderson Declaration's disgorgement figure was based on the average disparity between petitioners' sales price and the fair market value of the lots—$18,558—multiplied by the 466 lots known at the time to have been sold in violation of the Act. *Id.* at A6. This calculation yielded gross illegal profits of $8.65 million, the amount to be disgorged. *Ibid.* Petitioners produced no evidence to call that calculation into question.

Petitioners contend that the Henderson Declaration is hearsay and was therefore inadmissible on summary judgment. As the court of appeals concluded, however, the Declaration serves as a summary of voluminous evidence, and something like it "would doubtless have been permitted at a trial of the case." Pet. App. A10 (citing Fed. R. Evid. 1006).[7] The

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[7] Although the Henderson Declaration concerned the remedy rather than petitioners' substantive liability, the court of appeals analyzed the evidentiary question under the standards applicable to summary judgment under Federal Rule of

Declaration established the average sales price through the results of a survey of lot purchasers, corroborated by sworn declarations of a sampling of 11 purchasers. Pet. App. A10-A11. The average fair market value was established by HUD through records of the tax-assessed values of the lots, which the court of appeals held admissible under Federal Rule of Evidence 803(6). *Id.* at A11 n.10.[8]

HUD's case could have been proven at trial through the testimony of state tax officials and the testimony of each of the 466 purchasers, but in light of petitioners' failure to contradict HUD's evidence, such a showing was not necessary. As the court of appeals observed, "the practical question" was "whether the case present[ed] a genuine issue of fact for trial rather than whether the parties have put their evidence in final form." Pet. App. A10 n.8. HUD came forward with a reasonable method, based upon reliable sources of information, to calculate petitioners' total profits; in 27 months, petitioners failed to come forward with any evidence to contradict that calcu-

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Civil Procedure 56. Rule 56(e) requires that supporting materials on summary judgment must set forth facts "as would be admissible" at trial. In *Celotex Corp.* v. *Catrett*, 477 U.S. 317 (1986), this Court noted that Rule 56(e) is satisfied by submissions capable of being "reduced to admissible evidence." *Id.* at 327. Federal Rule of Evidence 1006 permits the admission into evidence of "a chart, summary, or calculation" when the contents of "voluminous writings * * * cannot conveniently be examined in court." Therefore, the court of appeals' analysis under the summary judgment standard was correct.

[8] Virginia law requires the tax assessments of real estate to be made at 100% of the fair market value. Va. Ann. Code § 58.1-3201 (Michie 1991). The district court found that the county assessments "establish[ed] with a high degree of certainty the fair market value of the properties." Pet. App. A38.

lation. See *id.* at A12 (noting that petitioner's evidence "is nil").

As for establishing the specific amount of funds that went to each individual petitioner, the district court held that "facts before the Court create a strong presumption that a substantial portion of CCMV's net earnings accrued as a result of its failure to comply with the Act's requirements," Pet. App. A44 n.7, and that this litigation "suggests that a substantial amount of profits passed to the individual defendants as a result of their violations," *id.* at A40. Nevertheless, the district court initially rejected HUD's proposal that the individual petitioners incur continuing joint and several liability for the entire $8,648,048 amount, *id.* at A44, and it allowed petitioners to offer evidence showing that part of that amount was not passed through CCMV to them, *id.* at A44, A70. As the court of appeals observed, "HUD and the district court doubtless envisioned that a searching inquiry into the individual defendants' finances would follow to see how much of the ill-gotten gains had flowed through CCMV and into their pockets." *Id.* at A9. Petitioners nonetheless disregarded the district court's repeated instructions to submit evidence and refused to respond to HUD's discovery or to produce documents that might have led to a more exact calculation. *Ibid.* Because of their default, they have no basis for complaint against the district court's calculation of the disgorgement award.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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